CHARTERED PROFESSIONAL ACCOUNTANTS CANADA

CPA Common Final Examination

BOARD OF EXAMINERS' REPORT

PART B — The Day 1 Report

September 2022 and September 2023 Examinations

CPA EVALUATIONS

CPA BOARD OF EXAMINERS MEMBERS

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See Part A for full report on the September 2023 Day 2 and Day 3 simulations and marking guides.

THE BOARD OF EXAMINERS' REPORT ON THE SEPTEMBER 2023 COMMON FINAL EXAMINATION

OBJECTIVES OF THE REPORT

The objective of this report is to explain the Common Final Examination (CFE) process and to assist the profession in improving the performance of candidates on the CFE.

The report sets out the responsibilities of the Board of Examiners, the methods used for guide setting and marking the CFE, and the results of the marking process. The report also includes recommendations to candidates from the Board of Examiners.

The September 2023 CFE Report is presented in two parts: Part A is the Day 2 and Day 3 report and Part B is the Day 1 report.

The appendices provide more detailed information on the design, guide setting, and marking of the CFE, as well as the board's expectations of candidates on the simulations. Readers are cautioned that the marking guides were developed for the entry-level candidate and that, therefore, all the complexities of a real-life situation may not be fully reflected in the content. The CFE report is not an authoritative source of GAAP.

RESPONSIBILITIES OF THE BOARD OF EXAMINERS

The Board of Examiners (BOE or the board) comprises a chair, two vice-chairs, and sixteen members appointed by the provincial bodies.

The board's responsibilities, as set out in its terms of reference, include the following:

- Setting the CFE in accordance with the *CPA Competency Map* (the *Map*) and other directions from the Professional Education Management Committee;
- Submitting the CFE and the marking guides to the provincial bodies for review;
- Marking the candidates' responses and recommending to the provincial bodies the pass or fail standing that should be given to each candidate; and
- Reporting annually on the CFE to various CPA committees and the provincial bodies, in such form and detail and at such time as is satisfactory to them.

The chair is responsible for the supervision of the evaluation process. A CFE subcommittee, made up of nine members of the board, is actively involved in the preparation of the CFE simulations, the preliminary marking guides, and the setting of the initial passing profile. The members of that subcommittee participate in the Preliminary Evaluation Centre where the marking guides are tested against candidate responses and finalized, and in the start-up of the marking centre. The BOE chair and vice-chair provide oversight throughout the entire marking process, consulting with subcommittee members as required. The full board is responsible for equating the difficulty of the examination to prior years' examinations and establishing the passing standard.

THE CFE

Preparation and Structure of the CFE

The board staff works in conjunction with authors to ensure that simulations presented to the board achieve the overall intent and design objectives set by the board, while adhering to the competencies and the proficiency levels specified in the *Map*.

The full board provides guidance as to the content and nature of simulations to be included on the examination. The CFE subcommittee reviews and refines these simulations that make up the three-paper evaluation set.

Nature of the Simulations

The CFE comprises a set of simulations that are both essential and effective in evaluating the candidates' readiness to enter the profession:

Day 1 – The first paper is a four-hour examination consisting of a single simulation that is linked to the Capstone 1 group case. There are two versions of the linked cases, unless special circumstances require that a third version be provided. Version 1 is linked to the most current Capstone case and is written by first time writers and by repeat writers who chose to attempt the new case rather than Version 2 of the previous Capstone case. Version 2 (and Version 3, if applicable) is written by repeat writers and candidates who deferred and are writing Version 2 (and Version 3, if applicable) as their first attempt. The versions of the exams are calibrated to ensure the difficulty of all versions is comparable. For the September 2023 CFE, a Version 1 and a Version 2 were offered. The Version 2 case relates to CFL, for which a Version 1 was offered in September 2022.

Day 2 – The second paper is a five-hour case, with four different roles and requirements. Additional information tailored to each role is provided in four separate appendices.

Day 3 – The third paper is a four-hour paper, consisting of three multi-competency area simulations.

Assessment Opportunities

The board applies competency-based marking procedures that enable it to decide which candidates demonstrate readiness to enter the profession.

Assessment Opportunities are designed to answer the question, "What would a competent CPA do in these circumstances?" To attain a pass standing, candidates must address the issues in the simulations that are considered significant.

Appendix A contains a comprehensive description of the evaluation process.

Marking Guides

Marking centre leaders and assistant leaders provide valuable input during the testing and setting of the marking guides, before live marking begins. The vice-chair, selected member(s) of the CFE subcommittee and senior evaluations staff hold meetings with the leaders and their assistants during both the guide-setting and the marking processes. See **Appendices B to F** for the CFL Day 1 simulations and related capstone case, CFL marking guides, and CFL sample responses. **Appendix G** contains the marking results by assessment opportunity, and **Appendix H** contains the BOE comments. A copy of the Day 1 V1 (JRP), Day 2 and Day 3 simulations can be found in **Part A** of the CFE Report.

Day 1 – The marking guide is designed to assess the candidate on the stages of the CPA Way: 1) situational analysis; 2) analysis of the major issues; 3) conclusions and advice; and
4) communication. Based on these four summative assessments, the candidate's response is then holistically judged to be either a passing or a failing response.

Day 2 and Day 3 – Marking guides are prepared for each simulation. Besides identifying the Assessment Opportunities, each marking guide includes carefully defined levels of performance to assist markers in evaluating a candidate's competence relative to the expectations set out by the board when developing the passing profile for a competent CPA.

Five categories of performance are given for each Assessment Opportunity. The candidate's performance must be ranked in one of the five categories:

- Not Addressed
- Nominal Competence
- Reaching Competence
- Competent
- Competent with Distinction

Setting the Passing Standard

The board chair and vice-chair in charge of the examination monitor the live marking. Near the completion of the marking process, the CFE subcommittee satisfies itself that the markers applied the marking guides as intended by the board.

In determining which candidates pass the CFE, a candidate is judged in relation to the board's pre-established expectations of an entry-level chartered professional accountant. Any changes to the initial profile that were made throughout guide-setting and the marking centre are ratified by the full board. In setting the passing profile, the board considers the following:

- The competency area requirements described in the *Map*
- The level of difficulty of each simulation (set using a scale: Easy, Easy to Average, Average, Average to Hard, or Hard)
- The level of difficulty of each Assessment Opportunity (set using a scale: Easy, Easy to Average, Average, Average to Hard, or Hard)
- The design and application of the marking guides
- Comments from leaders and assistant leaders regarding any marking difficulties encountered or any time constraints noted
- Possible ambiguity of wording or of translation
- Input on critical decision factors from an independent board (i.e., those BOE members not on the CFE subcommittee and therefore not directly involved) who review the fair pass package

The Decision Model

The purpose of the CFE is to assess whether candidates possess the competencies required of an entry-level CPA through a written evaluation that is common to all CPAs. Each day of the CFE is unique and is designed specifically to assess different skills:

- ➢ Day 1 is linked to the Capstone 1 group case work. It assesses the candidates' ability to demonstrate professional skills. It is independent from Day 2 and Day 3.

- Day 2 assesses technical **depth** in one of four unique roles (that reflect the four CPA elective choices) and provides **depth** and **breadth test** opportunities in the common core competency areas of Financial Reporting and/or Management Accounting. Candidates pre-select one role and respond from that role's perspective.

- Day 3 supplements the **depth** and **breadth** tests in the common core areas of Financial Reporting and/or Management Accounting, and also provides **breadth** test opportunities for all other common core competency areas.

Candidates must pass all three days in order to qualify for entry to the profession. Those seeking licensure must obtain depth in Financial Reporting and in the Assurance Role.

Day 1

Day 1 is assessed independently from Day 2 and Day 3. A pass or fail decision is made based on a holistic assessment of the candidates' performance in applying the CPA Way to demonstrate essential professional skills.

Day 2 and Day 3

The decision model used by the board is presented in Exhibit I. Four key decision points, or levels, are applied in reaching a pass or fail decision, as follows:

1. The response must be **sufficient**; i.e., the candidate must demonstrate competence in the Assessment Opportunities presented on Day 2 and Day 3 (Level 1).

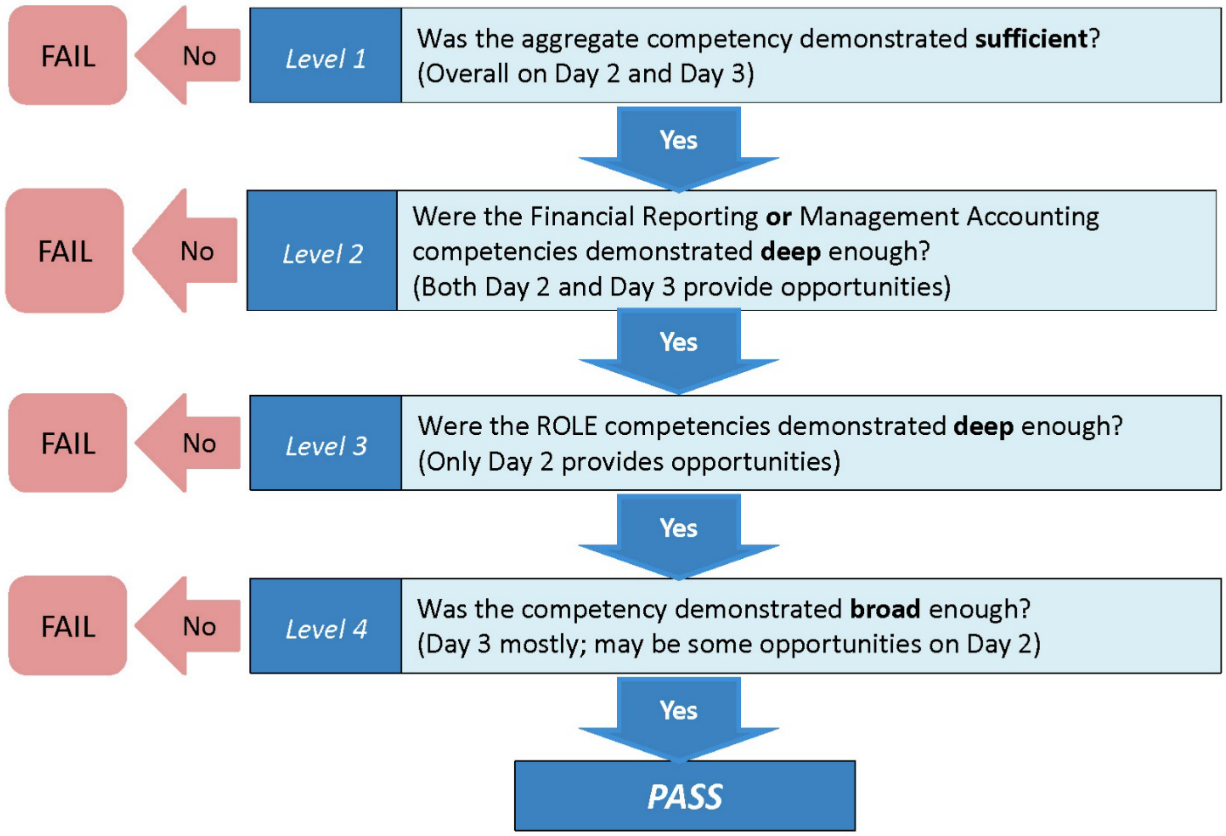
2. The response must demonstrate **depth** in the common core area of Financial Reporting or Management Accounting (Level 2).

3. The response must demonstrate **depth** in the pre-selected elective role (Level 3).

4. The response must demonstrate **breadth** across all competency areas of the *Map*, at a core level, by not having avoided a particular technical competency area (Level 4).

The BOE is responsible for equating the results from one examination to another to ensure that candidates have an equal chance of passing whichever examination they write. The BOE uses the factors listed above under setting the passing standard, in order to equate the examinations.

EXHIBIT I
DAY 2 AND DAY 3 PASS/FAIL ASSESSMENT MODEL



Approving the Results

The CFE subcommittee reviews and approves the marking results for each simulation. Day 1 is assessed separately from Day 2 and Day 3.

Day 1 – The CFE subcommittee discusses the profiles for both the marginally passing and marginally failing candidates to confirm that the board's pre-established passing profile has been appropriately applied by the markers.

Day 2 and Day 3 – As part of the development process, the CFE subcommittee sets preliminary requirements for the three levels (tests of depth and breadth) being assessed on the Day 2 and Day 3 simulations. After the marking is completed, the board reviews and finalizes those requirements. The board establishes the Level 1 (sufficiency) requirement for the combined Day 2 and Day 3 simulations.

During the approval process, the board continues to consider whether the results could be affected by any inconsistency in the evaluation or the board's processes.

Reporting

In reaching its decision, the board determines which candidates pass on a national basis only, without regard to provincial origin or language. Similarly, the detailed comments are based on analyses of the performance of all candidates.

The board reports the following information by candidate number:

- Overall pass/fail standing and pass/fail standing for each of Day 1 and of Day 2 and Day 3 combined.
- A pass/fail standing for Day 1.
- A pass/fail standing for Level 1, Sufficiency. A decile ranking is provided for failing candidates.
- A pass/fail standing for Level 2, Depth in Financial Reporting or Management Accounting.
- A pass/fail standing for Level 3, Depth in Role.
- A pass/fail standing for Level 4, Breadth in all technical competency areas.

Thank You

All board members wish to express their warm and sincere appreciation for the outstanding energy, support, and commitment of the Board of Examiners staff members whose dedication and talent contributed in large measure to the achievement of our objectives and the fulfilment of our responsibilities.

We also wish to acknowledge the contributions made by the provincial reviewers, markers, authors, translators, and editors. The commitment, energy, and skill demonstrated by all the markers were outstanding, resulting in the sound application of marking procedures and producing an appropriate evaluation of the candidates. Everyone's commitment to the quality and fairness of the process is appreciated.

Jonathan Vandal, CPA
Chair
Board of Examiners

A MESSAGE TO CANDIDATES

To attain a pass standing, candidates needed to achieve a "Pass" on Day 1, and on Day 2 and Day 3 combined, demonstrate sufficient competence in all areas and meet the two depth standards and the breadth standards.

Introduction

The September 2023 CFE Report, Part A and Part B combined, presents detailed information on all candidates' performance for all the examination cases, except for the Day 1 linked case, JRP Version 1. Detailed commentary on the performance of candidates on the JRP cases (Version 1 and Version 2) will only be available after JRP Version 2 is written in September 2024. The simulations, marking guides, marking results, and Board of Examiners' (BOE) comments on the Day 2/Day 3 portion of the examination are found in Part A of the CFE Report. Similar information on Day 1 CFL simulations (Version 1 and Version 2) can be found in Part B of the CFE Report.

The intent of this message from the BOE is to help candidates improve their performance on future CFEs by drawing their attention to the most common detracting characteristics observed in candidate responses to the September 2023 CFE. The BOE's comments are based on the feedback of the marking teams, who see the entire candidate population, and reflect the broad themes noted by the markers that apply to all candidates who wrote this sitting of the CFE. More detailed AO-by-AO commentary on candidates' performance can be found in the BOE's comments in Appendix F of Part A, or Appendix H of Part B, of the CFE Report.

Nature of the CFE

The design of the CFE is such that each day of the examination allows candidates to demonstrate a different skill set. Day 1 allows candidates to demonstrate their high-level professional skills, such as analysis that is relevant and critical to strategic decision-making, professional judgment, and ability to synthesize information. Day 2 allows candidates to demonstrate their technical competence in the common Financial Reporting and Management Accounting competencies and in their chosen role, which is tied to one of the four elective areas. Day 2 typically, but not always, directs candidates to the work to be done and is not designed to be time constrained, allowing candidates to demonstrate depth. Day 3 allows candidates to further demonstrate depth and breadth in the common Financial Reporting and Management Accounting competencies, and provides multiple opportunities to demonstrate breadth in all the other core technical competency areas. Day 3 is typically time constrained, requiring candidates to prioritize the issues and manage the amount of time spent on each issue.

Both Day 2 and Day 3 require candidates to integrate the information found in the simulation in order to demonstrate competence. All three days require candidates to clearly communicate their thought process.

Strengths and Weaknesses

Time management

Overall, candidates demonstrated good time management skills. The Day 1 simulation was not time constrained in any way and, generally, the amount of time that candidates devoted to their situational analysis and their issue analysis was appropriate. Most candidates were able to address all the strategic alternatives presented, spending more time on the alternatives that required more analysis and discussion. The Day 2 simulation was also not time constrained, and most candidates managed their time appropriately on Day 2, attempting all the AOs and appropriately balancing their time between the common section and the role section. On Day 3, which is designed to be time constrained and required time management on the part of the candidates, to ensure that all three simulations were completed within the four hours allotted, candidates seemed to be able to plan their time accordingly. There was some evidence of candidates running out of time, given the high average percentage of NAs (5%) on Day 3, Simulation 3; however, this is expected, given the design of Day 3.

Unrelated discussions

The BOE was pleased to see that there were relatively few unrelated discussions on this exam. Candidates addressed the requireds and generally did not provide any analysis that was not necessary.

Technical ability

The BOE has noted a trend of declining technical abilities. The pattern the BOE has seen for the past few CFEs has continued, with candidates generally avoiding the more complex topics. In addition, candidates struggled with most topics that had not been previously tested on the CFE, even though they are clearly testable, as outlined in the CPA Competency Map.

Candidates generally performed well on: Day 2, Assurance role, AO#9 (Procedures – accounting issues) and AO#12 (Procedures – compliance); Day 2, Finance role, AO#8 (Equipment NPV); Day 2, Performance Management role, AO#7 (Pea protein supplier), AO#8 (Just-in-time delivery), and AO#10 (Market survey analysis); Day 2, Taxation role, AO#7 (Capital cost allowance) and AO#9 (Taxable income); Day 3, Simulation 1, AO#2 (Federal corporate taxes payable), AO#4 (Understanding the audit plan), AO#5 (Solar power project options), and AO#6 (Appropriateness of vision, mission, and values); Day 3, Simulation 2, AO#1 (Grant and donation) and AO#5 (Cost allocation); and Day 3, Simulation 3, AO#4 (Governance structure and staff concerns). Many of these AOs contained topics that are regularly tested on the CFE.

However, on certain of the remaining AOs, there was more variability in the quality of the responses, with some candidates demonstrating a very poor understanding of the required technical knowledge.

On AOs requiring quantitative analysis, for example, on Day 2, Common, AO#1 (Inventory costing), many candidates did not incorporate the concept of equivalent units. On Day 2, Common, AO#3 (Variance analysis), candidates struggled to incorporate sales mix into their variance calculations. On Day 2, Performance Management role, AO#9 (Transfer pricing), many candidates either ignored the quantitative information provided in the case and attempted only a theoretical discussion of the potential transfer pricing methods, or attempted calculations using the data provided but failed to integrate them in their discussion of the potential methods, showing a poor understanding of the methods. On Day 3, Simulation 2, AO#3 (Financing options), and Day 3, Simulation 3, AO#1 (Upgrade options), candidates struggled to put the options provided to them on equal footing in order to compare them.

Candidates also demonstrated poor technical knowledge on some of the AOs that required Handbook or Tax Act knowledge. On Day 2, Common, AO#4 (Goodwill impairment), candidates struggled to correctly calculate the carrying value of the division and often did not know what to compare the carrying value to. On Day 2, Common, AO#5 (Note payable), many candidates did not recognize the main issue presented, which was the fact that the note payable contained a below-market interest rate and therefore needed to be adjusted to its fair value. On Day 2, Taxation role, AO#11 (Automobile benefits), many candidates used incorrect formulae to calculate the standby charge, and on AO#12 (Share sales), very few candidates identified that one of the transactions would result in an allowable business investment loss (ABIL). On Day 3, Simulation 3, AO#3 (CRA reassessment and acquisition of control), candidates were unable to provide the correct CRA reassessment time limit of three years, and demonstrated very little breadth of knowledge in explaining acquisition-of-control implications.

In addition, some candidates on this exam did not appear to use the reference schedule provided at the back of the exam booklet. For example, many candidates used the incorrect CCA class percentage on Day 2, Taxation role, AO#7 (Capital cost allowance), even though this information can be found in the reference schedule. In addition, on Day 2, Taxation role, AO#11 (Automobile benefits), candidates often used incorrect automobile rates (for lease limits and for calculating the operating cost benefit), or did not identify that the vehicle belonged to Class 10.1 even though it exceeded the limit for the year, and on AO#13 (Personal tax calculation), many candidates did not know how to use the personal tax brackets that were provided at the back of the exam booklet.

Candidates should expect to see a variety of issues of varying difficulty. The BOE encourages candidates to be balanced in studying, and to ensure that they have a sufficient level of technical knowledge in all competency areas that are outlined in the CPA Competency Map, as all topics in the Map are testable on the CFE. In addition, candidates should ensure that they are familiar with what is provided in the reference schedule on the exam, and ensure that the information is used when required.

<u>Failure to consider the specific context of the simulations and integrate the information provided</u>

Consistent with previous CFEs, candidates on the September 2023 exam seemed to struggle with applying the specific context of the simulation to their response. For example, on Day 2, Assurance role, AO#13 (Internal audit plan), many candidates provided an external audit planning memo, even though it was clear that the candidate was in the role of internal auditor. On Day 2, Finance role, AO#13 (Selling price (sell or hold)), candidates discussed the shareholder agreement but only did so generically, and did not tie the discussion to the specific scenario of Treadstone wanting to exit now. On Day 2, Performance Management role, AO#11 (Salespeople compensation plan), candidates often provided generic discussions about the theory of what is being tested, and did not incorporate any specific case facts in their discussions. On Day 2, Performance Management role, AO#13 (Treadstone’s objectives and operational improvements), candidates often simply noted that the objectives were “met” or “not met,” without explaining why and incorporating case facts. On Day 3, Simulation 2, AO#6 (Key performance indicators), many of the key performance indicators provided by candidates were generic or did not consider the not-for-profit context of the case.

The BOE emphasizes that the ability to adapt to unique scenarios and integrate information from various parts of the case are important skills for an entry-level CPA. In addition, the role of the CPA is often to advise clients, either on the application of standards and tax rules or on why, and how, to proceed with certain business and financial decisions. Without a clear explanation, a client would have incomplete information. In the case of responses to CFE simulations, the BOE is interested in understanding the logic used and is looking for evidence of the analysis and professional judgment that was applied in reaching a conclusion. Therefore, it is important for candidates to answer the questions “Why?” or “So what?,” using case facts when making any point, and to include the answer in the response. Jumping to the conclusion without first presenting the analysis supporting that conclusion is insufficient. The BOE is looking for a clearly articulated response.

Pre-populated financial information

On the September 2023 exam, any financial information presented in the case that had 10 lines or more was provided to candidates electronically in the exam-writing software. This was done for the first time in May 2023. Similar to May 2023, the BOE was pleased to see that many candidates took advantage of this and leveraged what was already provided, to save time and/or provide a more structured response. However, the BOE purposely included an AO on the exam with a bigger dataset (Day 2, Assurance role, AO#11 (Equipment subledger – anomalies and procedures)), and had expected candidates to use the exam-writing software to electronically perform data analysis on the information provided to them. Surprisingly, it appears that many candidates did not do this. The BOE reminds candidates that data analytics is an important part of the CPA Competency Map, and that the financial information is being pre-populated in order to allow candidates to perform data analysis in a more comprehensive and efficient manner.

For more detailed commentary, see Appendix F of Part A of the CFE Report.

Additional Comments Specific to Day 1 – JRP (Version 1)

Most candidates dedicated the first section of their response to a relevant situational analysis. Most used this information later in their response, making relevant links back to the company's global situation when analyzing the specific strategic issues that were presented, and within their conclusions. However, the links that weak candidates made were typically to the more obvious case facts that related to JRP's key success factors, mission, and vision, rather than being tied to the more important factors such as the downturn in the economy and the board's investment objectives.

Within the simulation, there had been a downturn in both the Canadian and global economies and, as a result, the board's main investment objectives had changed, and JRP's board would give preference to investments that provided JPR with the highest annualized return on investment (ROI), but they were also only comfortable with making low-risk investments. Internally, JRP only had $500,000 of cash available for strategic investment, and a potential loan of up to $7 million. Candidates were expected to integrate the critical elements of the company's broader situation, including the downturn in the economy, the board's objectives, and JRP's cash constraint, within their qualitative and quantitative analyses of each strategic alternative.

For each of the strategic alternatives available to JRP, candidates were expected to conclude and recommend a course of action that was consistent with their analyses. Within their conclusions, candidates were expected to discuss and integrate the board's main investment objectives, as well as respect the amount of capital the company had available for strategic investment.

There were five strategic alternatives to be analyzed in this case: whether to open two additional premium dog camps or sell BALA; whether to install a pet pharmacy within JRP's existing stores; whether to partner with Pet Fresh to create a premium pet box delivery service; whether to become the exclusive Canadian distributor of PPC's pet medicines and pharmaceuticals; and whether to offer an advanced dog training program, Training+.

Within the analysis of the major issues, three main factors differentiated strong responses from weak responses. First, a strong response identified and provided an in-depth discussion on the most important decision factors for each issue. Weak candidates tended to list case facts, often failing to explain why those elements were important and how they affected the decision-making process. Second, strong candidates provided valuable quantitative analyses to help support their recommendations (such as by linking their calculations to the stated objectives of JRP). On the other hand, weak candidates' quantitative analyses were often unstructured and unclear and, therefore, challenging to follow. Many weak candidates also failed to perform the correct calculation, to adequately assess each issue. These candidates often struggled to explain how the results of their quantitative analyses affected the decision at hand. Third, strong candidates routinely linked their analysis of each option to the prevalent entity-level issues presented in the case: the board's objectives; the impact of the economic downturn; and the cash constraint facing JRP. Strong candidates incorporated these aspects into their discussion of each strategic alternative, whereas weak candidates either missed making these links altogether or provided a superficial discussion that failed to adequately highlight the significance of these aspects in relation to each of the strategic decisions that needed to be made. Strong candidates also often recognized the inter-relationships between the strategic alternatives, such as the fact that the Training+ program was an inadvisable investment if the company decided to sell BALA.

Weak candidates tended to only perform an issue-by-issue analysis, without stepping back to consider the broader perspective, and without integrating the key entity-level issues into their conclusions. As a result, they failed to make important links between the various aspects of each alternative. For example, weak candidates attempted to calculate the ROI of each option but did not then compare them to each other, and so failed to adequately address one of the board's main investment objectives.

Most candidates approached their response in a coherent and organized fashion. Only a few candidates struggled to effectively communicate their ideas. These candidates tended to use poor sentence structure, confusing syntax, and an unorganized approach to their response.

Additional Comments Specific to Day 1 – CFL (Version 2)

Similar to JRP Version 1, most candidates dedicated the first section of their response to a relevant situational analysis. Most used this information later in their response, making relevant links back to the company's global situation when analyzing the specific strategic issues that were presented, and within their conclusions.

In addition to considering the board's objective of increasing and diversifying the company's sources of revenue, candidates should have also highlighted the major issue relative to CFL's internal environment within their situational analysis: the board's expressed intention to step back from the active involvement in CFL's day-to-day operations within roughly five years. As a result of this intention, CFL's board only wanted to make low-risk investments that were simple to operate and that provided a stable and reliable source of revenue. In addition, CFL only had $6.5 million of cash available for strategic investment, with no access to further financing. Candidates were expected to integrate these critical elements of the company's broader situation into their analysis of the major issues.

There were five strategic alternatives that candidates were expected to analyze both qualitatively and quantitatively: whether to acquire Iron Depot; whether to sign a hotel gym management contract with Sunnyside Hotels; whether to engage RiseEd to help create and distribute streaming fitness videos; whether to develop and operate physiotherapy clinics; and whether to open additional PurCafés.

Similar to JRP Version 1, strong candidates recognized and discussed the most important decision factors for each issue, provided valuable quantitative analyses, and linked their analysis to the significant entity-level issues presented in the case. Strong candidates tended to incorporate the assessment of whether the alternatives were low-risk and simple to operate throughout each of their issue-by-issue discussions, and within their conclusions and overall recommendations. Strong candidates also recognized that there were interrelationships between the investment recommendations they made and CFL's existing and potential future operations. For example, strong candidates recognized that Iron Depot had supplier contracts that would allow CFL to purchase equipment for the company's existing fitness facilities at a 20% discount.

One of the main differentiating factors between strong and weak candidates was the ability to identify and discuss in depth the most relevant aspects of each strategic alternative presented as part of their analysis. Rather than discuss the more pertinent implications, weak candidates' analyses tended to focus on the minor considerations. For example, for the PurCafé alternative, weak candidates tended to focus their analysis on the alignment between offering healthy food and the company's mission, vision, and core values, instead of the fact that it is low-risk because there were already PurCafés that were operating and profitable. Weak candidates also often did not step back and consider the entity-level issues within their analysis of the strategic alternatives.

As was the case with JRP Version 1, only a few candidates struggled to effectively communicate their ideas. These candidates tended to use poor sentence structure, confusing syntax, and an unorganized approach to their response.

APPENDIX A

EXAMINATION DESIGN, MARKING GUIDE DEVELOPMENT, AND MARKING OF THE COMMON FINAL EXAMINATION

CFE Design

Day 1 is one four-hour case that is linked to the Capstone 1 case, which is worked on in groups for eight weeks prior to the CFE. When writing the Day 1 case, candidates are allowed access to their Capstone 1 case but not their group's answer or any sample response. The Day 1 case is designed to assess the enabling (professional) skills. Candidates are directed to target a "board room and senior management" level of discussion, with high-level analytics and a strategic focus. There are typically two versions of the Day 1 case. Candidates pre-select the version they will write.

Day 2 is one case designed to be completed by an average candidate in three and one half hours that candidates are given five hours to respond. The extra one and one half hour gives candidates time to filter and find the information that they need to answer *their* role requirements from within the common information presented. Day 2 is designed to assess the technical competencies in **depth** (Level 2 and Level 3). Candidates pre-select a role (Assurance, Finance, Performance Management, or Taxation). All candidates work with the same case — it has a common section and four sets of appendices containing additional information applicable to each of the four unique roles. The required tasks, regardless of the role, are clearly directed unless there is an undirected/enabling issue in the case that the board expects candidates to identify on their own. Day 2 evaluates the competencies listed in the *CPA Competency Map* mostly in the elective area and in common Financial Reporting and/or Management Accounting areas in **depth** and **breadth**. The role **depth** test (Level 2) may also include coverage of other competency areas from the common core.

Day 3 is a four-hour examination containing a mix of small cases (75 to 85 minutes each[1]) that evaluate the common core competencies only. The Day 3 cases provide additional opportunities for **depth** and **breadth** in Financial Reporting and Management Accounting and provide **breadth** opportunities for all the other technical competency areas. Cases are time constrained, and they are designed to cover different competency areas within each case. A higher level of integration and judgment is required on Day 3 of the CFE than in the core modules, although the technical competencies are tested at the common core level of expectation.

The assessment opportunities on the Day 2 case are given mark values such that each of Day 2 and Day 3 are weighted equally.

[1] The CFE Blueprint allows anywhere between 45 to 90 minutes. The September 2023 CFE ranged from 75 to 85 minutes.

The Development of Marking Guides and the Provincial Review Centre

Prior to the Common Final Examination being published, provincial reviewers, appointed by each region, meet to examine the simulations and the preliminary marking guides. The provincial reviewers' comments are then considered by the board when it finalizes the examination set and again when the leaders and assistant leaders review the marking guides in the context of actual responses at the Preliminary Evaluation Centre.

The September 2023 CFE Evaluation Centre

The September 2023 CFE Evaluation Centre was run with both in-person and remote components. From the marker applications received, approximately 210 individuals were chosen to participate in the September 2023 CFE marking centre. The criteria for selection included marking experience, motivation, academic achievement, work experience, personal references, and regional representation. The marking was supervised by the CPA Canada CFE full-time CFE professional staff, with oversight by the CFE subcommittee vice-chair, and the chair of the BOE.

The Day 1 Version 1 linked case (JRP V1) was marked by a team of 26 people from October 5 to 20, 2023. The Day 1 Version 2 linked case (CFL V2) was marked by a team of six people from September 21 to 28, 2023.

The Day 2 Common assessment opportunities were marked separately from the role assessment opportunities by a team of 36 people from October 1 to 15, 2023. Day 2 Assurance was marked by a team of 39 people from October 1 to 17, 2023. Day 2 Performance Management was marked by a team of 14 people from October 2 to 14, 2023. Day 2 Finance was marked by a team of four people from September 19 to 25, 2023. Day 2 Taxation was marked by a team of three people from September 20 to 26, 2023. All three Day 3 cases were marked from October 5 to 21, 2023. The Day 3 simulations were marked by a total of 82 people.

In advance of the marking centre, the members of the CFE subcommittee, staff, leaders, and assistant leaders participated in a three- to six-day preliminary evaluation centre (PEC). Participants reviewed the marking guides, applied them to randomly selected candidate responses, and made necessary revisions to the marking guidelines, taking into account the comments on the marking guides received from provincial reviewers.

The larger teams followed a set marking centre schedule, which included a start-up phase to train the markers. During the start-up phase, the leaders and assistant leaders presented the marking guides to their teams, while staff and the BOE vice-chair monitored the discussions. The teams undertook a two-phase test-marking procedure prior to actual marking. Phase one consisted of marking guide familiarization, during which markers applied the marking guide to copies of candidates' responses and collectively reviewed their results. Phase one thus ensured that all markers understood the issues in the marking guide and the basis on which to apply each expectation level. Phase two consisted of an expanded test marking of several responses to establish marker congruence.

After the training and test-marking phases, and only when marker congruence was achieved, live marking commenced. All larger teams had a leader, and anywhere from one to five assistant leaders, and had both French-speaking and English-speaking markers. Each team had one or more markers who marked in both languages.

For smaller teams, all markers attended PEC, and moved directly from PEC to live marking. These teams had a leader, and two to five experienced markers, of which two were bilingual and marked all the French papers. These bilingual markers started in English and switched to marking in French once their marking was assessed as being consistent with the team. The bilingual markers arbitrated the French papers by discussing where there were differences in their markings. If they were unable to agree on a final assessment, the bilingual markers translated the relevant portions of the response for the team leader, and the team leader made the final assessment.

The board strives for the highest possible marking consistency and quality control. Leaders and assistant leaders, therefore, devoted much of their time to cross-marking and other monitoring activities. Control papers were fed into the system daily to check marker consistency. Markers' statistics were reviewed to ensure that marking remained consistent throughout the centre. Based on analysis of the statistics, leaders reviewed and, if necessary, re-marked papers to ensure that the assessment opportunities were marked fairly for all candidates. Bilingual markers marked papers in both languages, and their results were compared to ensure that the marking was consistent in both languages. Additional audits were performed at the end of marking on any of the larger differences between markers.

Borderline Marking (Day 1)

Each candidate's paper was marked once. All candidates' responses that were assessed as clear fail, marginal fail, or marginal pass were marked a second time by the team leader, an assistant team leader or a senior marker. Clear pass results were also audited to ensure accuracy of marking.

Double Marking (Day 2)

Each candidate's Day 2 paper was marked independently by two different markers. If the two initial markings differed on any assessment opportunity, an arbitrator (the leader, an assistant leader, or a senior marker) compared the two initial markings and determined the final assessment.

As an added measure to ensure that markers were consistently applying the marking guide, a two-day rule exists, which results in the second round of marking not beginning until two days have elapsed since the first marking. Adherence to this rule ensures that any movement in the application of the marking guides due to marker interpretations during the first two days of live marking are stabilized before the second marking and arbitration process begin.

Borderline Marking (Day 3)

Day 3 was marked using a borderline model. All Day 3 responses were marked once and then the Day 2 and Day 3 results were combined. All failing candidates who passed the Day 2 role test, had their Day 3 response marked a second time by an independent marker, and any differences between the first and second markings were arbitrated by a leader or senior marker.

Subsequent Request for Remark of Results and Request for Performance Analysis

Failing candidates may request a remark of their examination results and/or a detailed personalized performance analysis for either Day 1, or Day 2 and Day 3 combined, or for all three days for a fee.

Applications must be forwarded to the Board of Examiners through the provincial bodies. If a candidate wishes to apply for a remark of their results and/or a detailed performance analysis, they should notify their respective provincial bodies within the specified time limit indicated in the results letter.

In an effort to provide failing candidates with more timely feedback, the Board of Examiners is providing an automated feedback report for Day 1 of the CFE. The report is automatically generated using the marking data collected for each response rather than being based on a personalized review of the response and is being provided at no cost to all failing candidates. This report is intended to allow for the identification of the key deficiencies in the candidate's Day 1 response, which then allows the candidate to decide whether to request the more detailed, and personalized performance analysis report noted above, for a fee.

Remarking of Results Approach

Great care is exercised in the original marking and tabulating of the papers and results. The following procedures are applied to all three papers constituting the Common Final Examination.

Under the supervision of the chair of the Board of Examiners and of CPA Canada CFE staff, the responses are reviewed by the leaders and assistant leaders who did the original marking. The leaders and assistant leaders read the responses and compare them to the marking guides used at the marking centre. In reviewing candidates' results, two aspects are considered. First, it must be determined that the basis of marking the papers has been consistent with that accorded other candidates who wrote the examination. Second, all responses reviewed are subjected to a careful check to ensure that the markers have indicated that consideration has been given to all material submitted by the candidate.

The results are tabulated, and a decision made as to whether any candidates have been treated unfairly and should be granted a pass on the examination.

The results are then forwarded to the provincial bodies for notification of the candidates.

APPENDIX B

CAPSTONE 1
CFL BACKGROUND CASE

Capstone 1

CanDo Fitness Ltd. — Case (FOR REFERENCE ONLY)

Candidates are expected to use the case facts from the Capstone 1 case to complete their analysis. It is not expected that students consider the impact of emerging current events (such as the COVID-19 *pandemic) in their response. However, candidates may choose to do so in a reasonable way. For instance, when conducting industry research, candidates may encounter and consider the implications of* COVID-19 *on the industry. However, the impacts of current events (including* COVID-19*) are not meant to be a significant part of candidates' analysis.*

It is April 15, 2022, and you have been working as a CPA with Serringers Consulting Group LLP (SCG). You have been assigned to develop a report for the board of directors and management of CanDo Fitness Ltd. (CFL).

CFL has approached SCG with a request to assist with strategic analysis and to set a new direction for the company. Based on past years' results, the board is concerned about the declining members, revenues, and profits. There are conflicting viewpoints among the five shareholders as to how the company should grow in the future, as well as many operational issues that CFL would like you to analyze and address.

You have been provided with the following information to review and analyze. (All dollars are Canadian dollars unless specifically stated otherwise.)

CanDo Fitness Ltd.

CFL owns and operates fitness facilities in Western Canada. Currently it has 40 locations, which average 10,000 to 13,000 square feet each, with total annual revenue of $46 million and earnings before taxes of $1.1 million for 2021. The company is owned by five shareholders: the founder, Phillip Rogers, owns multi-voting shares, giving him 60% voting power, and the four remaining shareholders, Sandra MacCarthy, Brian Mitchell, Frank Chang, and Rosa van der Schuren, each has 10% voting power. The five shareholders share equally in the equity interest of the company. The company's mission is to help members achieve their fitness goals and to promote healthy living.

The company had been successful until 2017, when increasing competition created pricing wars, reducing membership and requiring the company to cut prices and costs. Since 2018, membership, revenues, and profits have been falling. There is now disagreement on the future direction. Some of the shareholders want to grow quickly to a size where CFL can achieve some economies of scale, compete on price, and keep a traditional gym format that provides consistency at all locations. The other shareholders believe that the company should try to differentiate by providing different programs and services that will attract new target customers. They believe it is important to provide different options to members, rather than each gym being exactly the same. They want to change with the trends.

An organizational chart is provided in Appendix I. CFL's most recent financial statements for the years ended December 31, 2019, 2020, and 2021 are provided in Appendix II. Industry benchmarks are provided in Appendix III.

Industry information

Description and size

The gym, health, and fitness facility (fitness) industry in Canada consists of operators of fitness and recreational sport facilities that provide exercise and other physical fitness conditioning or recreational sports activities, such as skating, swimming, or racquet sports. It also includes facilities that provide fitness instruction.[1] Total industry revenue is $4.5 billion, and the annual growth rate to 2025 is expected to be 4.6%.[2]

The industry is in a growth cycle as the benefits of a healthy lifestyle continue to be publicized and supported by government and corporate programs. Revenue is earned in the fitness industry from the following segments:[3]

Revenue source	Percentage	Notes
Membership fees	69.4%	Membership fees are generally monthly, although some companies now bill every two weeks or weekly, allowing customers to easily cancel their memberships, thus reducing sales. Smaller boutique fitness studios also sell memberships via individual class passes. High turnover and shorter membership periods are driving operators to generate revenue from other sources to reduce their reliance on membership fees.
Personal training services	10.9%	This segment of revenue is increasing, and the trend is to hire accredited trainers for personal training and classes.

[1] Ediz Ozelkan, "Break a sweat: Rising health concerns and incentives from businesses will increase demand," *IBISWorld Industry Report 71394C: Gym, Health & Fitness Clubs in Canada*, March 2019.
[2] Ozelkan, 2019.
[3] Ozelkan, 2019.

Revenue source	Percentage	Notes
Amusement and recreation services	5.9%	This segment includes revenue from recreational activities, such as skating, climbing walls, and bowling. These types of services are not common within the industry, and therefore, those that do provide these services have little competition.
Fitness and recreational admission	3.3%	Includes one-time fees for special events that are held at the facilities, for example, competitions.
Food and beverages	2.7%	Includes sales of juices, shakes, snacks, and other food items.
Athletic instruction	3.0%	Includes fees collected for coaching and training for specific sports.
Spa services	2.3%	Includes spa services, such as facials and massages, offered at the facilities.
Other	2.5%	Includes sales of apparel and accessories, and late fees and penalties.
Total	100%	

Customer segments

Females account for 40% of all memberships, and this proportion has been increasing over the past years with the increase of female-only fitness facilities.[4]

The primary customer segments by age and their respective percentages of revenue for the industry are as follows:[5]

Customers aged 55+	35.0%
Customers aged 40-54	20.0%
Customers aged 20-39	27.9%
Customers aged 19 and younger	17.1%

Customers in the two older segments (that is, those who are 40 years of age and older) tend to be more health conscious, have more disposable income, and represent a large segment of the general population. As well, over the past five years, fitness facilities have started to target the seniors' market (customers aged 55+), offering low-intensity exercise programs, yoga, and aerobic activities.

[4] Ozelkan, 2019.
[5] Ozelkan, 2019.

Consumers aged 20-39 have been the traditional target segment for this industry, but this is changing. Although this segment has not grown over the past years, 50% of individuals in this age group do participate in some form of physical activity.

The customer segment for consumers aged 19 and younger has become a growing segment in the industry as obesity in children is becoming a chronic problem. Parents are looking for fitness alternatives as schools cut back on physical education programs. About 70% of individuals in this age segment participate in physical activity.

Consumers generally choose to become a member of a fitness facility based on factors such as the following:[6]

- Cost: The price of a membership, and any extras that will have to be paid.
- Member profile: The type of people that are current members, such as female only, professional athletes, and so on.
- Equipment and programs: The type of equipment provided, such as cardio, weight machines, and dumbbells, and the quantity of each type. This also includes the availability of any programs and classes, and whether any are specialized to appeal to a certain segment.
- Busyness: The peak hours and how crowded the gym is at these times. Members tend to prefer facilities that are not too crowded, so there is sufficient space to exercise and less distractions and wait time for equipment.
- Extras: The availability of extra features, which might include daycare, massage and other spa services, tanning, juice and snack bars, nutritional counselling, and so on. The cost of any of these extra features or whether they are included with membership fees.
- Accessibility: The location of the facility. Members will often choose a facility that is close to their home or place of work.
- Cleanliness: The overall cleanliness of the facility, and the cleanliness policies in place.
- Maintenance: The general state of the equipment. Members want the equipment to be in excellent working order.
- Hours of operation: The hours and days the facility is open, such as whether it is open 24 hours, open on weekends and holidays, and so on. Members tend to prefer facilities that are open longer hours.
- Personal training: The availability of personal training, the qualifications and experience of the trainers, whether the trainers are readily available, whether the trainers provide individualized training programs, and whether the personal training is an extra fee.

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[6] Shannon Clark, “Top 10 Things To Look For When Choosing A Gym,” Bodybuilding.com, April 29, 2019, https://www.bodybuilding.com/fun/sclark32.htm.

- Membership privileges: The membership privileges that are available, such as any extra services offered at the facility for free or at a discounted rate. In some cases, memberships may also provide a discount at local stores or restaurants.

Competition

Competition is high and increasing. It is based primarily on price, customer service, brand recognition, and types of services offered.[7] Fitness facilities are local businesses and therefore competition is in the local markets. It is critical in this industry to have easy access to members, have multiple locations, offer a wide range of services, and effectively promote products and services.

The industry is fragmented, with 7,922 establishments across Canada. Goodlife Fitness Centres Inc. (Goodlife), a Canadian private company, is the largest operator of fitness facilities, with 1.5 million members, 400 locations across Canada, and 18.7% of the market share.[8]

Barriers to entry are very low, as shown by the following statistics:[9]

- 50.5% of the industry is made up of self-employed individuals (non-employee establishments) offering fitness facilities and classes.
- 33.3% of industry operators have less than five employees, and 25.3% employ between five and nine employees.

At one end of the industry spectrum are the multinational and national large operators that have brand-name recognition and multiple locations, who are continuing to expand to gain economies of scale. At the other end of the industry spectrum are the smaller, local niche players that cater to the local customer.[10] Taking into account all types of operations (including the self-employed), more than 80% of all establishments have fewer than 10 staff, and it is these small, boutique operations that impede the larger establishments from gaining significant market share.

The profitable commercial operators compete against non-commercial operators such as the following:[11]

- Non-profit and government fitness facilities (for example, YMCA locations or municipal community centres) that have the advantage of being able to get real estate at a lower cost.
- Hospital, corporate, and apartment building facilities, which have the competitive advantage of being conveniently located either at the member's place of work or their home, and, in some cases, are provided at no or very low cost to the member.

[7] Ozelkan, 2019.
[8] Ozelkan, 2019.
[9] Ozelkan, 2019.
[10] Ozelkan, 2019.
[11] Ozelkan, 2019.

- Home gyms, which are outfitted by fitness equipment suppliers. In this case, individuals build their own home gyms that give them the convenience to work out whenever they want, on equipment that is always available, with no crowds.

Competition can be segmented on price. This is especially true for the traditional "big-box" gyms that provide a large variety of equipment and classes. For example, some facilities are low-cost, low-amenity gyms. These facilities may also have no staff during off-peak hours, particularly if they are open 24 hours. These fitness facilities offer low or no initiation fees and low monthly rates. They attract budget-conscious customers, students, first-time gym goers who are not yet convinced that this is for them, or people wanting to join only for a specific season.[12] In fact, one low-budget facility has monthly fees that are so low that its business model assumes that people will not bother to cancel their memberships, even if they are not attending on a regular basis — and this seems to be successful.[13]

These budget-friendly gyms, which provide high-value, low-price health facilities, have seen significant growth by attracting members with low-priced memberships of $10 to $20 per month. These low rates appeal to customers who want to join for shorter periods of time. At the same time, these gyms provide a greater variety of equipment and classes, giving a better value proposition in comparison to traditional fitness facilities.[14]

At the high end are luxury facilities that are exclusive, are high priced, and offer many extra amenities and services to appeal to customers looking for niche services. Additional amenities might include stocking all-natural products in the change rooms, providing eucalyptus-scented chilled towels, having a fireside lounge, and offering smoothies.[15] These types of fitness facilities attract members who are willing to pay for these special services or exclusivity or who want fewer crowds when they are working out.

Competition can also be segmented based on products and services provided. The trend is for fitness facilities to become specialized and move away from offering only general fitness classes. Fitness facilities may provide a wide range of products and services, including spinning, aerobic, and yoga classes; weight training; a swimming pool; and racquet sports. For these types of facilities, equipment includes cardio and weight equipment.

Boutique studios have also seen significant growth. The boutique studios are small and specialized and provide limited services such as spinning, high-intensity interval

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[12] Ozelkan, 2019.
[13] "Fitness Industry Analysis 2020 - Cost & Trends," Franchise Help, accessed October 20, 2020, https://www.franchisehelp.com/industry-reports/fitness-industry-analysis-2020-cost-trends/.
[14] Ben Midgley, "The Six Reasons The Fitness Industry Is Booming," *Forbes*, September 26, 2018, https://www.forbes.com/sites/benmidgley/2018/09/26/the-six-reasons-the-fitness-industry-is-booming/#75c369bd506d.
[15] Amanda Vogel, "The Top 10 Fitness Trends for 2019," *Best Health*, January 7, 2019, https://www.besthealthmag.ca/best-you/fitness/2019-fitness-trends/.

training, barre, and Pilates. These boutiques are higher priced at $150 to $200 per month or $20 to $50 per class, but their value proposition is smaller classes, specialization, and a “quaint” atmosphere that appeals to people who are looking for friendship and support.[16] These boutique fitness facilities were originally located in high-density city centres but are expanding to smaller city centres in order to increase their members and number of locations.[17]

Facilities may also be niche operators, specializing in a limited number of products and services such as CrossFit, Olympic boxing, martial arts or yoga studios, spinning, climbing and bouldering walls, or any other type of physical activity. These niche operators might require specialized equipment.

Included in this niche segment are the facilities where serious athletes train as professionals or semi-professionals; they require a high level of training expertise on site.[18] These serious athletes have very specific preferences depending on the nature of their sport and are not influenced by price, customer service, or brand recognition in selecting which fitness facility to join.[19] Additionally, these specialty training centres can have a very dedicated fan base, with members[20] truly believing in this particular type of fitness activity and building their entire lifestyle around it. This community-like behaviour at these specialty facilities can also provide alternative sources of revenue generated from inter-facility competitions and the sale of branded merchandise.[21]

Competition can also be segmented based on size. Increasingly, the larger, better-financed operations have expanded nationally (and internationally) to achieve economies of scale and brand recognition. These big companies have the resources to spend substantial dollars on advertising and to provide heavily discounted initial membership rates to attract new members. The smaller, local operators, who cannot compete on price, have the advantage of being locally known and thrive by catering to their local community and tailoring programs to meet local needs.[22]

Finally, with respect to competition, some of the multinational competitors grow by using a franchise model, where, as the franchisor, they provide the business model and setup to franchisees in return for an upfront franchise fee and ongoing percentage of revenues earned by the franchisee. Planet Fitness Inc. is an example of a company that uses this model.[23]

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[16] Midgley, 2018.
[17] “Fitness Trends for 2019,” Perfect Gym, December 31, 2018, https://www.perfectgym.com/en/blog/club-owners/fitness-trends-2019.
[18] Ozelkan, 2019.
[19] Ozelkan, 2019.
[20] “Fitness Industry Analysis 2020.”
[21] “Fitness Industry Analysis 2020.”
[22] Ozelkan, 2019.
[23] “Annual report (10-K) for the year ended December 31, 2018,” Planet Fitness Inc., accessed October 20, 2020, https://investor.planetfitness.com/investors/financial-information/sec-filings/2018/default.aspx.

Currently, companies from outside of Canada do not have a substantial market share in the Canadian fitness industry. For example, LA Fitness International LLC has 2.9%, Anytime Fitness (Self-Esteem Brands LLC) has 1.7%, and Planet Fitness Inc. has 0.8%.[24] However, although the current market penetration in Canada is small, it is expected that these companies will increase their geographic scope and penetration in the Canadian market. These multinationals are well financed with proven business models and economies of scale, making them a key competitor for the future.

Wages represent 37% of revenues. Having trained employees is important for success, although the mix of part-time and full-time employees can vary greatly within a company. There is a shortage of skilled and experienced fitness instructors and trainers. Currently, the larger national and multinational competitors attract the most highly skilled people since they also pay benefits for their employees and wages slightly higher than minimum wages. The minimum wage across Canada is also expected to increase in the near future.

Regardless of the business model followed by companies, in order to be successful, companies in this industry need to have clean facilities with good-quality equipment and good customer service. Retaining members is also vital for success, which includes being innovative to meet the ever-changing demands of these members.

Demand drivers

Demand is determined by household disposable income, consumer confidence, amount of available leisure time, weather and seasonality, attitudes and trends toward healthy living, obesity rates, ability and desire to participate in sports, and the cost and availability of these services and their substitutes.[25]

Trends within the fitness industry

- Fitness facilities are trying to differentiate based on individualized customer service to increase customer retention and reduce churn rates (that is, attrition rates). For example, in a large health facility chain survey, the biggest complaint by far was general service.[26]
- As health insurance costs increase, some employers and insurers now cover the costs of health facility memberships to reduce insurance costs.[27]
- As people become more conscious of the foods they eat and move toward more healthy eating habits, a natural progression of this is that they become more interested in overall health and keeping fit.[28]

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[24] Ozelkan, 2019.
[25] Ozelkan, 2019.
[26] Stuart Goldman, "Data Mining the Health and Fitness Industry," *Athletic Business*, January 2016, https://www.athleticbusiness.com/apps-software/data-mining-the-health-and-fitness-industry.html.
[27] Midgley, 2018.
[28] Midgley, 2018.

- The increased use of wearable fitness trackers (such as Fitbit, Apple Watch, and Garmin), allowing people to monitor calories burned, heart rate, and steps taken, has provided additional motivation for people to improve their levels of fitness.[29]
- The increased use of fitness apps that provide video and audio prompts for a multitude of exercise routines has allowed consumers to work out at home and not attend a gym, thereby saving the payment of a gym membership.[30]
- There has been an increase in good streaming options for people who are too busy to go to the gym or whose schedules don't fit the timing of classes. Streaming allows people to train at home, but not by themselves. For example, with Peloton bikes, people can join virtual spinning classes. Peloton sells equipment that is fully equipped for streaming videos, and then sells a subscription to the videos and livestreams. In many cases, however, the people who stream classes at home are also still members of fitness facilities.[31]
- Outdoor obstacle races and other forms of inter-facility competitions are becoming popular. These races and competitions are often all ages, and since participants need some place to train, this has influenced the growth rate of fitness facilities. Inter-facility competitions generate team spirit and a feeling of being part of a community, which keeps people coming to the facility to be with their friends and for the comradery.
- As the baby boomers age, they want to maintain their health and are drawn to fitness facilities to do so.
- As cardiovascular disease rates in the population continue to rise, fitness plays a large role in keeping the population healthy, increasing the demand for fitness facilities.
- Historically, members have signed one-year contracts, and facilities have charged cancellation fees if contracts are terminated early. However, with increased competition, gyms have begun to offer more flexible membership terms, even offering one-week and two-week memberships. These shorter contracts lead to more volatility in a company's revenues.[32]

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[29] Midgley, 2018.
[30] "Worldwide Survey of Fitness: Where the Fitness Industry is Headed," Technogym, accessed October 20, 2020, https://www.technogym.com/int/newsroom/worldwide-survey-fitness-industry-trends-2019/.
[31] Midgley, 2018.
[32] Ozelkan, 2019.

- The industry is increasingly using data analytics to understand members and keep track of trends.
  - Part of GoodLife's success, as stated by its owner, is: "GoodLife has stayed ahead by closely tracking trends in fitness facilities and adapting to outwork the competition."[33]
  - Data analytics are gathered from member surveys and by tracking members' visits in an effort to improve customer satisfaction and reduce churn rates. Information such as where members live, what they do, how far they travel to the gym, how often they come to the gym, and what programs they use is also gathered. All of this information is then used in combination with survey results to determine how best to retain members and anticipate churn rates.[34]
- There is a trend toward hybrid establishments that provide one-stop shopping, appealing to millennials. These establishments include casual eateries that provide nutritious meals along with a variety of fun and challenging fitness programs.[35]
- There is an increasing need for community and shared experiences. Within the fitness industry, consumers are more interested now in boutique fitness facilities that provide more personalized, expert instruction and services and create a sense of community.[36]
- There is the trend toward more meditation studios to allow consumers to slow down and recharge. As a result, fitness facilities are also providing these types of spaces.[37]
- New apps allow consumers to try out different classes around the city and avoid having to pay membership fees, for example, ClassPass or Hussle. The advantage for fitness facilities in giving these types of passes is they can attract new members. The advantage for consumers is that they get to try out new classes and locations at discounted prices.[38]
- With the increased use of technology, there is a greater demand for fitness facilities to digitally transform their spaces to enhance their connectivity with users. This means that fitness facilities should have their own mobile app to allow users to book classes or memberships on the go and to provide their trainers or the facility with updated information on their progress from their wearable devices. These apps can

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[33] Hank Daniszewkski, "London-based GoodLife Fitness Founder David Patchell-Evans vows to defend his fitness turf from U.S. invaders," *The London Free Press*, September 29, 2016, https://lfpress.com/2016/09/29/london-based-goodlife-fitness-opens-new-headquarters-plans-to-grow-even-more/wcm/660dbedf-c570-a7d0-fef3-c01291ea9660.

[34] Rosemary Counter, "How GoodLife Fitness focused on reputation and data to grow massively across Canada," *Canadian Business*, January 10, 2019, https://www.canadianbusiness.com/lists-and-rankings/best-managed-companies/goodlife-fitness-best-managed-companies/.

[35] "4 Reasons Why Fitness Is Booming in the Business World," Socialnomics, March 4, 2019, https://socialnomics.net/2019/03/04/4-reasons-why-fitness-is-booming-in-the-business-world/.

[36] Peloton Interactive Inc., Prospectus filed August 27, 2019, https://www.sec.gov/Archives/edgar/data/1639825/000119312519230923/d738839ds1.htm.

[37] Vogel, 2019.

[38] "Fitness Trends for 2019."

then be used to gather data that can be further analyzed to assess which classes are most popular, examine users' behaviours to estimate their churn risk, and provide individualized discounts or offers to members to increase retention.[39]

- There is an increasing general trend for businesses to be "green" and reduce their impact on the environment. In fact, 73% of millennials are willing to pay more for environmentally responsible practices. In the case of the fitness facilities, this entails taking initiatives to reduce water usage and electricity. Some of the initiatives that are being taken include capturing the energy that is produced on bikes and elliptical machines to power the facility; using and selling eco-friendly supplies; reducing water consumption by having low-flow showerheads, toilets, and faucets; using efficient lighting and temperature controls; and going paperless.[40]
- The trend for churn rates for the majority of Canadian fitness facilities is close to 50%, which is extremely high. Operators are using social media and face-to-face interactions with members to lower these rates. In addition, those facilities that offer additional services tend to have lower churn rates.[41]

General risks in the fitness industry

- Product and service risk: The company must provide the classes, equipment, and environment that will appeal to members. Revenues are primarily based on memberships, and there is the risk that current members will not renew. The company will not be able to attract new members without the right products and services being offered.
- Location risk: Location is an important contributor to success of a fitness facility. The facility must be situated within close proximity of its target membership. Therefore, the lack of suitable sites could slow growth and revenues.
- Health and safety risk: One of the greatest risks for a fitness facility is that a member will be injured in a class or while using equipment. This could result in a lawsuit requiring significant amounts of cash to settle and destroying the company's reputation.
- Compliance risk: The company must also comply with regulations related to health and safety. Statutes and regulations have been implemented to give members the right to cancel their contracts, generally allowing members to cancel their membership contracts within 10 days after the commencement date with refund of amounts paid. In addition, initiation fees cannot be more than twice the amount of annual memberships and any food, drug, or supplements sold must be approved by Health Canada.[42]

[39] "Fitness Trends for 2019."
[40] Jenny Weller, "10 Ways to Create an Environmentally Friendly Gym," Glofox, October 25, 2019, https://www.glofox.com/blog/10-ways-to-create-an-environmentally-friendly-gym/.
[41] Ozelkan, 2019.
[42] Ozelkan, 2019.

- Reputational risk: The company's name and brand could be damaged as a result of many types of incidents.
- Technology risk: Failure to safeguard members' data is a risk. Fitness facilities store and transmit members' information related to banking and personal data. There is the risk that this confidential information could be compromised.

Company background

CFL was established in 2002 by Phillip Rogers, a world-class cyclist and an advocate for fitness and healthy living. He was well known at that time in Canada for his placement in the Tour de France and other world-class cycling races. Phillip became frustrated with the local gyms and the lack of services and amenities offered, prompting him to open his first fitness facility in Vancouver, B.C. Phillip's goal was to have a fitness facility that would appeal to all types of people, not just serious athletes. He also wanted a place that would provide a wide variety of classes and equipment that could be used by members in customized fitness programs and where members could feel comfortable and not be judged on their appearance or level of fitness.

The 12,000 square foot fitness facility was designed to have cardio equipment (treadmills, ellipticals, steppers, and cross-trainers), weight-training equipment, and two large workout studios — one for a spinning class and one for a variety of aerobic and weight-training classes.

Phillip used his name as an elite athlete to promote and market his facility. The first facility became very successful, attracting a significant number of members. Phillip knew that his presence was important for the image and brand of the company, so he could be seen regularly at this facility working out and joining the group classes.

Unlike many competitors, CFL's strategy was not to set targets for its employees related to the number of new members, and commissions were not paid on bringing in new members and achieving targets. Phillip's philosophy was to have the gym be a fun and friendly environment and not to pester people about renewing their memberships or bringing in new members.

Based on the success of this first facility, Phillip decided to expand to other locations in Vancouver and the surrounding areas. By 2007, CFL had 10 different locations. However, Phillip was having difficulty going to each facility on a regular basis and decided that he needed some other people to help with this. He wanted known local athletes who would provide some genuineness to the facilities and enhance the brand recognition.

As such, CFL ownership expanded to include four new shareholders who are world-renowned athletes: Sandra MacCarthy (rowing), Brian Mitchell (rock climbing), Frank Chang (boxing), and Rosa van der Schuren (skiing). These individuals also have a passion for healthy living and fitness activity. To complete the issuance of new common shares to these four new shareholders, CFL changed its capital structure to include

Class A multi-voting common shares that had six votes per share and Class B common shares that had one vote per share. Phillip was issued 1,000 Class A multi-voting common shares, which gave him six votes per share (6,000 votes total), and each other shareholder was given 1,000 Class B common shares with one vote per share. In total there were 4,000 Class B common shares issued. Each Class A multi-voting share can be exchanged for a Class B common share, and Class A and Class B shares each have the same economic value and equity interest in the company.

The four new shareholders initially agreed to this share structure because the company's success had been tied to Phillip, and Phillip had invested the time and funds to grow the company and build its brand to date. At the time, giving Phillip control did not appear to be an issue as the shareholders were very interested in investing and all shared the same vision for the company. Therefore, these terms were accepted.

With the addition of the new shareholders, the company decided to expand to Alberta, since two of the shareholders lived in this province. In 2009, the company opened three locations in Calgary, duplicating the model previously used in B.C. Expansion continued in Alberta and B.C., and in 2016, the company had a total of 35 locations across these two provinces. In 2017, the company expanded to Manitoba, opening five new fitness facilities.

Initially, the reputation of the facility was built on having elite athletes working out at each location. Each shareholder was given eight locations and committed to attending each location at least twice a week to work out and be on hand to talk to members. Members really enjoyed this and appreciated seeing these well-known athletes. At the same time, the shareholders gained first-hand knowledge of what was going on at each location. The other benefit of this was that new members would be attracted to the gym based on the fact that a "famous and elite" athlete was also working out at their gym. This was a key marketing tool and an important factor in differentiating the company from other local facilities. It was this differentiating factor that allowed the company to grow quickly in its earlier years.

Company overview

CFL currently has 40 fitness facilities: 20 in B.C., 15 in Alberta, and five in Manitoba. Although size varies between 10,000 to 13,000 square feet each, each location has the same setup and follows the same business model as the original facility. Today, the company has 49,800 members in total, with members per location varying between 680 and 1,365. The facilities are open 24 hours a day, 365 days a year. Classes are only offered during the morning and evening times. Facilities are unstaffed between 9 p.m. and 6 a.m. Revenues are earned from memberships and the sale of personal training hours.

Phillip's original philosophy and approach to the facilities are still adhered to today — the gyms are to be welcoming and nonjudgmental, regardless of an individual's level of fitness or their reason for working out. Consistency is key since members can visit any gym they want to, and Phillip wants members to feel immediately at home no matter which location they visit. Therefore, all facilities provide the same types of classes and equipment, and the layout of each facility is the same. Aerobic and weight-training classes are held in one room and spinning classes are held in a second room. Cardio and weight machines take up the rest of the space, in addition to change rooms. Memberships cover the use of the facility, all classes, and a towel service. Staff do not try to sell new memberships, and commissions are not paid on signing up new members. An important component of the employees' job is to be friendly and converse with the members.

Within each facility, fitness instructors provide group class instruction for aerobics, weight training, and spinning. Members may also purchase personal training hours to work individually with a trainer, to help them achieve their goals. The personal trainer will initially meet with the member to understand their goals, and then design a fitness program that will help the member to achieve their goals. Then, each time they meet, the trainer will motivate the member and ensure that they are doing the program safely and correctly.

In the past, the company would provide educational classes for members on a variety of nutrition, behaviour, and fitness topics, but due to cost constraints, these have not been offered since 2017.

CFL is not large enough to achieve economies of scale, so it cannot effectively compete based on price against the larger market players, and it continues to rely on its ability to differentiate itself by providing "elite athletes" as members. However, as the shareholders aged and reduced the amount of time spent working out, their visits slowly declined. Today, only two shareholders, Phillip and Sandra, visit locations in B.C. on a regular basis. Brian, Frank, and Rosa only visit a facility once a month, if that. In addition, as the shareholders have aged, their reputation with potential members, who are younger, has declined to the point where new members do not recognize their names.

Up until 2016, CFL made a point of supporting community events that promoted health and fitness. It hosted community fitness events at each facility that were open to the entire local community and sponsored rising local athletes. Due to ongoing cost constraints, these community events are no longer held. Because of these changes and the shareholders' declining reputations, the company's name is no longer well recognized in the local community.

Corporate vision and mission

CFL's vision and mission statements, approved by the board in 2017, are:

Vision statement: *To provide the means to motivate and help adults to achieve their goals.*

Mission statement: *We are a company dedicated to educating and motivating adults to embrace a fit and healthy lifestyle in a friendly and nonjudgmental atmosphere, providing state-of-the-art equipment and innovative, fun, and challenging group classes. We also strive to further develop health and wellness in the local communities.*

Corporate values

CFL has five main core values, also approved by the board in 2017, as follows:

1. All employees are caring and understanding of members and work as part of a team to meet the corporate goals and mission. Members, guests, and staff are treated with honesty, dignity, and respect at all times.
2. We continuously update our equipment to ensure that it is leading edge and provide ever-changing group classes that stay up to date with the current trends. We provide unmatched service by having uniquely qualified and passionate staff.
3. All staff are committed to their own fitness goals and healthy living and are able to motivate members to do the same.
4. We strive to build a community of friends in a safe and supportive environment and to be a driving and vocal force in the local community to promote fitness and healthy living.
5. We provide activities that are fun, challenging, and designed to help individuals achieve their fitness goals.

CFL also has a code of conduct and a code of ethics implemented in 2016, which stipulates that all staff will act ethically. Employees may anonymously report any potential violations of this code of ethics, which management commits to investigating immediately.

Future plans and objectives

In March 2022, the board met and set the following objectives:

- Increase total revenues by 10% by 2025.
- Increase the earnings before interest, taxes, depreciation, and amortization (EBITDA) margin to 25% of revenues by 2025.
- Increase the total number of members by 15% by 2025, and target a new customer segment.
- Improve members' level of overall satisfaction and reduce the churn rate to less than 30% by 2025.

Company structure

The board of directors meets every month and is made up of the five shareholders. At the meeting, the board members discuss topics related to financial reports and budgets, operational and staffing issues, financing issues, and election of the officers. The company has been paying dividends since 2015. There are no formal board committees.

The shareholders also have a shareholders' agreement. As part of the shareholder agreement, Phillip has five votes at the board meetings and all other directors have one vote each. One clause in the agreement states that in certain circumstances, the shareholders and board members are given equal voting rights regardless of the multi-voting status of some of the shares or other stipulations in the shareholder agreement. This condition is invoked for change of control and other special shareholder resolutions. A second clause in the agreement relates to exiting. This exit provision allows a shareholder to offer a specific price per share to purchase the shares of other shareholders. The other shareholders are then required to either accept the buy-out offer or purchase the shareholder's shares at that price per share.

Management team

CFL's corporate management team is made up of the following individuals:

Phillip Rogers — chair of the board and chief executive officer (CEO)

Phillip is 47 years old and was a world-class cyclist from 1996 to 2006. He is an advocate for fitness and healthy living. He has a bachelor of physical education that he earned in 1999, and he lives in B.C. He is passionate about being fit and healthy and motivating people to embrace these same beliefs, and he makes a point of visiting all of CFL's fitness facilities at least twice per year. Phillip is very friendly with staff and members. Members that know him or have met him are impressed with his level of fitness, and he is a model for a fit and healthy lifestyle. Phillip is a strong believer in visiting the gyms, talking to members, and trying to attract new members with existing members' referrals. Because he thinks members are more important than staff, he spends a very limited amount of time with staff when he visits the gyms.

Phillip is convinced that the company has to grow. He has lamented that CFL has not grown since 2017 and believes that this is the major problem. He believes that CFL needs to be bigger in order to reduce its operating cost per member and that it needs to rapidly expand to accomplish this. Phillip has become impatient over the past five years and feels that now the company needs to make up for lost time.

Sandra MacCarthy — VP human resources

Sandra is 42 years old and was a world-class rower, competing for Canada in several Olympics. She has known Phillip for many years, and it was because of this friendship and mutual respect that Phillip asked if Sandra would be interested in becoming a shareholder in 2007. Phillip's wife is Sandra's best friend, and therefore Phillip and Sandra socialize outside of the company.

Sandra has a degree in business and before joining CFL she worked in human resources for an insurance company for about eight years. Sandra has always led a fit lifestyle and today is still involved in coaching the rowing team at one of the local universities. Since she is diligent about working out, she also continues to visit many of CFL's facilities in B.C., which is her home.

Sandra is a good listener, and when she visits CFL's facilities, she meets with the manager and staff to understand their concerns. Sandra has been finding that she not only has to handle employee issues, but that members will often call her or corner her at the gym with concerns that they have about staff, especially in situations where the local manager has not been helpful. Sandra tries to treat everyone fairly and respectfully.

Sandra hires and terminates all the management staff. The gym managers report directly to Sandra on employee-related issues. Although the managers have direct responsibility for hiring and terminating staff at the local level, Sandra sets and approves the wage rates that are paid to the individuals and is responsible for all employee benefit plans.

Sandra supports Phillip's viewpoint that CFL needs to expand rapidly to catch up with the other competitors. She believes that CFL has a good model but just needs to grow to reduce per-unit costs.

Brian Mitchell — VP marketing and IT

Brian is 49 years old and was an elite rock climber, scaling rock faces and mountains all over the world until he had a serious accident about 10 years ago. He has been involved in making many documentaries about his climbing feats. Brian has a degree in engineering, but has more recently taken many courses in computing, website design, and social media, which are now his primary areas of interest. As a result, Brian has been key at implementing CFL's marketing and IT strategy. Brian is a strong believer in market research and spends a lot of time researching competitors and trends in the fitness industry online. He believes the company could make more use of its data if it had the proper systems to gather, collect, and analyze the information.

Brian's preference is to research and understand all the issues before making decisions, and he believes that only with complete information can an appropriate analysis and decision be made. He has clashed with Phillip over many decisions.

Brian believes that an understanding of the fitness industry trends and competitors is vital to CFL moving forward with the right strategy. Brian wants the company to focus on the niche market and move away from the consistent, generic format of the facilities, instead focusing on providing speciality services that are attractive to specific segments of the industry. He wants the format of the facilities and programs offered to vary location to location, based on the needs of the local community and the local competitors.

Frank Chang — VP equipment and programs

Frank is 52 and was an elite boxer in his younger days. Prior to joining CFL, Frank worked with a U.S.-based fitness equipment distributor, holding a variety of different positions, including sales manager and purchasing manager. He still uses these old contacts to get the best equipment prices for CFL. He spends a lot of time visiting equipment suppliers and trade shows to keep abreast of the next generation of equipment, which is ever-evolving, and this doesn't leave much time to visit CFL's facilities.

Each year, Frank has an off-site meeting with the managers to discuss new and replacement equipment at each location. He is committed to keeping the equipment as state-of-the-art as possible, and his goal is to have equipment that is not more than three years old, though he is not always successful.

Although Frank is technically responsible for the group classes that are provided at each facility, he leaves it up to the local managers and fitness instructors to determine the class schedules and the nature of the classes provided. Since the actual type of class cannot be changed, the only thing that can vary at each location is how many of each type of class will be offered and certain elements within the class itself.

Frank understands that the company has been performing poorly, but he primarily blames it on the group classes. He would like to see a reduction or elimination of general classes and instead see different types of equipment or amenities added at the locations, depending on local needs.

Rosa van der Schuren — chief financial officer (CFO)

Rosa is 45 years old and was a world-class skier. Her hometown is Calgary, where she spends a lot of time in the mountains in the winter months, coaching and racing. In the off-winter months, Rosa will periodically visit CFL's different facilities to discuss membership rates and budgets with the managers. Rosa has a master's degree in business administration and worked in the finance departments of two large public companies before joining CFL. She joined CFL because she wanted a private company where she could be involved in day-to-day financial decisions. She is responsible for the annual budgets, monthly financial reports, and year-end reports. She also handles all banking matters and all issues related to real estate, including lease agreements and finding new locations.

Due to family commitments, she works out regularly at home and only rarely works out at the local CFL facility. Rosa determines membership rates, controls how many free passes will be allocated to each facility per year, and authorizes membership discounts. She has the final authority to approve all expenditures and signs all cheques (which also require a second signature from any of the current shareholders).

Rosa is very concerned about the declining membership numbers and the membership fees. She has already told the directors that they cannot lower annual fees below $600, given the existing membership numbers, but the new rate has been approved to be $590. She believes that drastic changes need to be made because currently about 10 locations are performing poorly. If changes are not made, these locations may have to close in the next few years.

Rosa has also suggested that the company cut its dividends. She would like the shareholders to take less in salary, which is currently at $300,000 per year, per shareholder, and use these funds to adequately pay the fitness instructors. However, the shareholders have all come to rely on their annual salaries (which are significantly higher than market rates) and their dividend payments.

Human resources

The company has just over 1,200 employees. About 78% of the employees are part time and 22% are full time. In the last two years, staff turnover has increased to 20%, as the younger, newly hired employees tend to leave in less than two years. The company has been able to retain some of its older fitness instructors and personal trainers who have been with the company for more than 10 years. Historically, the company had about 50% full-time employees, but as long-time staff retired or left, they were replaced with part-time staff. Due to a shortage of skilled and experienced labour, the part-time staff are usually less qualified and less experienced, and are therefore paid less than the full-time employees.

The part-time staff, consisting of the group fitness instructors and front desk staff, are paid the minimum wage as required by the province in which they work. The group fitness instructors require either some limited experience or minimal certification. There is high turnover among the group fitness instructors.

The personal trainers are well trained and experienced and are paid an annual salary.

The breakdown of employees is as follows:

Senior management — shareholders	5
Other senior management	3
Gym managers	40
Group fitness instructors	920
Personal trainers	160
Front desk staff	52
Administration, marketing, IT, head office staff	30
Total employees	1,210

The personal trainers all have non-compete clauses that prohibit them from working for any other competitors. They are also not allowed to take on any personal business opportunities that arise through the use of CFL’s property, information, or position. This means that the personal trainers cannot take on their own clients and be paid directly, nor can they personally profit from outside services provided to these clients, which includes selling third-party products. Group fitness instructors may also not work for a competitor, unless there is prior approval from one of the shareholders of the company.

Other employment policies are summarized as follows:

- All employees must behave ethically and treat everyone with respect, courtesy, and fairness.
- CFL is committed to providing a safe and healthy workplace, and employees are required to follow all safety and health regulations and report any accidents immediately.
- Employees are not to discuss or share any member or company confidential information with anyone outside the company. Privacy of members' data should be protected at all times.
- All employees are given a free membership to the fitness facilities and 10 guest passes annually.

In a recent employee survey, 85% of the fitness instructors were highly dissatisfied with their compensation and benefits. The fitness instructors have been complaining for the past year that they are not being paid for all their hours worked. The current practice is to only pay for the length of the class that they teach. They are not paid for time to prep, set up, and take down any equipment required for the class or for any time spent chatting with the class attendees or answering questions. Since all staff are there to promote the facility, the fitness instructors are constantly being told by management to come early and stay after class to talk to the members. In addition, they do not receive any paid sick days. Although Sandra has brought these concerns to the other shareholders, there hasn't been any action taken to deal with this growing issue.

Currently, the shareholders take a combination of dividends and salary as compensation, which has been the policy for many years. Rosa is wondering whether this is the right mix and what they should consider in making this decision.

Company operations

Revenue

Members sign a one-year contract that outlines the monthly payment required and how the payment will be made. Fees are payable monthly and collected directly with authorized direct payment from the member's bank account or a monthly charge to the member's credit card. Therefore, the company has no accounts receivable. There are no upfront initiation fees required. CFL does not offer monthly memberships or a fee-per-use option.

The membership fee provides members with access to all locations (not limited to one facility), all group classes, and towel service. CFL's strategy has been that a single fee structure keeps everything simple for members and avoids confusion. The company has not reduced the number of group classes offered even though attendance has been declining as the membership declines.

In April 2022, annual membership fees were decreased to $590, due to reduced pricing by local competitors. Members can pay for personal training programs, which are charged separately at $90 per hour.

Over the past three years, revenues have been earned as follows:

	2021	**2020**	**2019**
Membership fees			
2021 — 50,750 members × $620*	$31,465,000		
2020 — 52,240 members × $635*		$33,172,400	
2019 — 54,800 members × $650*			$35,620,000
Personal training revenues	14,735,000	14,987,600	14,439,000
Total revenues	$46,200,000	$48,160,000	$50,059,000

*This amount represents the average annual fee for the period.

The company's current members range between the ages of 14 to 55, with about 70% being between 40 and 55. In addition, about 48% of the membership is female. The company's churn rate for 2021 was 55%, which has increased from 2018 when it was 28%.

Member surveys have provided the following feedback in the past:

- Members appreciate the simple fee structure and access to multiple locations.
- The facilities were rated high for cleanliness.
- The personal trainers were rated as friendly, knowledgeable, and good motivators.
- The fitness instructors, overall, were rated as very poor. Based on additional comments provided, members complained that the staff were unfriendly, disinterested, and not very motivational.
- Although the cardio and weight equipment were rated as good, group class offerings were rated as poor because they were outdated. Members want to see new and different amenities and programs offered.
- Members would prefer to have the option of shorter contractual periods, such as biweekly or monthly, rather than annual contracts.
- Members are leaving to join niche fitness facilities that offer speciality programs or because they can get similar facilities and services for a cheaper price at a competitor.

The company does not sell any goods or other products.

Property, plant, and equipment — net

(in '000s)		**Amortization policy**
Land and building	$ 6,780	Straight-line over 30 years (building)
Leasehold improvements	13,212	Straight-line over 20 years
Furniture, fixtures, and equipment	21,718	Straight-line over 2 to 8 years
	$41,710	

CFL owns its head office land and building, which it purchased seven years ago, and it has 40 leases for its fitness facility locations (all classified as operating leases). CFL's fitness facilities are all located in residential areas with large target markets within a 10-minute drive radius. Since CFL has a reputation for being a stable operator, landlords have been willing to provide leases initially for 10 years, with two five-year renewal options, at CFL's discretion. Assuming the renewal options are all taken, the company's leases will expire between 2024 and 2037.

CFL purchases and owns all its equipment used in the fitness facilities. One of the company's primary goals is to provide high-quality fitness equipment from leading suppliers and to ensure that the equipment is well maintained and replaced or updated on a regular basis. The cardio equipment has mounted colour TVs, links to MP3 players, headphones for the TV, and internet capabilities. CFL usually invests between $4 million and $5 million annually in new machines, of which up to $4 million is for cardio equipment and up to $1 million for weight equipment. Increasingly, the useful life of the cardio equipment is getting shorter, requiring increasing investments to keep the equipment up to date.

Marketing and advertising

CFL relies heavily on word of mouth advertising, attracting new members through referrals from its existing members. As a result, CFL provides a discount to any existing member who brings in a new member, equal to 7% of the new member's fees for six months, which is provided as a reduction in the existing member's fees. Members are made aware of this referral program through posts on social media, emails to members, and posters at the facilities.

As is common practice in the industry, the company will give free gym passes for the day to consumers interested in joining. As well, in January, when New Year's resolutions prompt new members to join, CFL gives away discounted annual memberships for a limited period of time. These free passes are not recognized as costs, and the discounts given on memberships are recognized as lower revenues.

The company uses its website and social media to promote its business. CFL has a well-maintained and user-friendly website, which has a members-only portal for booking classes and personal training sessions and for making payments. The website is also used to attract new members, is easy to navigate, and provides extensive information about the facility locations, hours, and facilities. The company is also on Facebook and Instagram, where CFL posts its semi-annual marketing campaigns. Personal trainers and fitness instructors are also featured on the website and on Facebook. The company tracks how effective its marketing campaigns are by noting the number of new members that sign up as a result of a specific initiative.

Data analytics

CFL has personal data collected on individual members, such as age and gender. Another database system tracks data for each member on how often they come, what time they come in, and which classes they attend. In addition, the company sends out surveys to its members and accumulates the results of all the responses. The systems that gather this data are all independent and there is no ability to cross-analyze any of the information. CFL currently does not use any data analytics programs, but these programs have been used by competitors to better analyze the results of collected data, to increase retention, reduce churn rates, and improve member satisfaction.

Financial reporting and budgeting

CFL prepares its financial statements using accounting standards for private enterprises (ASPE). CFL's bank, Gold Financial Bank (GFB), requires audited annual financial statements, which have been prepared by Fuller, Wilkinson & Co. LLP for the past 10 years. The audit for 2021 was completed in March 2022.

Banking and financing

CFL has the following line of credit and long-term debt outstanding, both with GFB:

1. Line of credit: Maximum limit of $1,500,000, bearing interest at prime plus 2% (prime is currently 2.5%). The line of credit is secured by a general security agreement. Currently, there are no funds withdrawn on this line of credit.
2. Mortgage payable: The 6% mortgage is secured by the property, plant, and equipment. It is repayable in annual principal payments of $2,500,000 on July 1, and matures on June 30, 2025. The mortgage has two covenants: the total-debt-to-EBITDA ratio (total liabilities divided by EBITDA) cannot exceed 4.2 and the EBITDA-to-interest ratio (EBITDA divided by interest) cannot be less than 4.0.

The company has found two alternative sources of funds for any new long-term investments. The terms and conditions proposed for each alternative are provided in Appendix IV.

Board meeting dialogue

The board met on April 13, 2022. Prior to the meeting, a briefing was distributed to the board members on the four new projects that had been discussed at earlier meetings:

- acquisition of Mighty Fitness Inc. (MFI) (Appendix V)
- proposal for indoor climbing wall facilities (Appendix VI)
- entering into distributor and video contracts with Zenfit Equipment Co. (Appendix VII and VIII)
- proposal to develop PurCafés in five gym locations (Appendix IX)

The meeting's agenda was announced as follows:

1. Consider the four proposed strategic alternatives.
2. Discuss any other business.

Excerpts from the discussions that took place are detailed below.

Phillip: Thank you all for coming. As you know, we are at a serious point in time for the company, and we will have to make some significant decisions about our future strategy. We decided at an earlier board meeting that we would analyze our members' data to determine what an appropriate mix of classes by location might be.

Brian: That's correct. I think SCG can assist us with some of our data analytics. We have three separate systems that gather a tremendous amount of data that is not currently being used to its potential. I would like to be able to take a member's personal data, blend it with data on gym and class attendance, and then blend it with the survey results from that member and see what we get. I think that this information could be used to provide better customer service, helping us to retain more current members and to assess what classes we should be providing at which locations. I would like to pilot this analysis at one of our Vancouver locations. Depending on what information we can gather, we can then decide whether we would like to roll out the data analytics initiative to our other locations. I have provided details on CFL's current data collection and storage processes (Appendix X). I also had IT pull the relevant source data from our three systems, and this information is included in the following Excel files: AttendanceData*, MemberData*, and SurveyData*.

Phillip: Yes, we can certainly ask them. We will consider changes to class offerings at a future date, once we have this data and a chance to discuss it further. For now, the rest of this meeting is to look more broadly at other available strategic options. I think I have a solution that I am very excited about. Last week, I had a phone call from a long-time friend, Gino Rossi. As you might already know, Gino is the sole shareholder of the fitness company MFI, which owns and operates gyms throughout Ontario and Nova Scotia. He has run into some cash flow problems and has decided to sell 50% of his company for $12 million. He is offering it to CFL first, since he knows me personally and thinks this might be a good fit. Gino has provided me with some preliminary information on his company (Appendix V).

Brian: What are his cash flow problems?

* NOT INCLUDED

Phillip: He has a long-term loan coming due later in 2022, and although the bank has agreed to renegotiate it, they have already said that the interest rate will be 10%, which will be a huge increased cost for Gino. He borrowed this debt originally to open his last five gyms three years ago and to buy new equipment. Right now, the bank is charging him 8%. He is looking for a partner to provide some cash, which he will use to pay down the debt. He would also like a partner since he is finding it difficult to manage the entire business on his own.

Sandra: The price is really good for what we would be getting. I like the idea of being able to expand to a bigger size quickly and being able to say that we are now “national.” Merging the two companies would enhance our reputation and allow us to compete better with other national competitors.

Phillip: I totally agree! This is a really unique opportunity that we cannot pass up. I have known Gino forever, and he is an astute businessman and very well connected in the fitness industry. His chain of gyms is growing, and he told me that he has grown his membership base by 6%, even before adding in the new members from the new locations.

Brian: I see from his website, which is really well done, that he has a unique method of providing classes using the equipment rather than the basic traditional forms that we use. This is definitely at the forefront of the industry trends. They also do training programs for competitions like the Mudder[43] races.

Sandra: His gyms are also very colourful and well decorated. I am guessing that we could use his flair for colour and decorating in our facilities to make them trendier. This acquisition would also give us access to a younger customer base.

Frank: We are only buying 50% of the company, so how will we be able to exert control?

Phillip: Gino says that he will give us two seats on the board, and he will only have one.

Frank: But why would he give up control in this way? Are you sure there isn’t something that we are not being told? I am not really interested in making any risky acquisitions.

Phillip: I think he is just desperate to get the cash into the company and pay down his debt. I have a feeling that if the cash cannot be raised, he may have to close some of his locations, although he has not stated this in these exact words.

Rosa: From my quick analysis, it appears he has grown too fast in the past few years and has not managed his cash flow very well. I am not sure we would be able to control

[43] The Mudder series of races include the Tough Mudder races and others. These are endurance obstacle course races of varying distances and difficulty. See https://toughmudder.com/events/all-event-types.

his spending so that he doesn't get into a similar position again, especially if he is left to oversee the operations. I don't think we should pursue this acquisition.

Frank: I am also concerned about the two different cultures of the companies. MFI is known as a trendy gym and we are known as a traditional gym. I am wondering if our brand reputation might be tarnished in some way. I don't think our members would be attracted to these types of gyms.

Rosa: If we pursue this acquisition, we might end up as a company that has two different brands appealing to two different markets and therefore have to manage these both separately, which would be difficult to do.

Phillip: This is a cost-effective way for us to grow and expand. We have to grow in order to compete with the national competitors. With our control of the board, we should be able to make changes that we want at MFI. MFI has great locations and favourable leases, and this is where I think we need to expand.

Brian: Are you proposing to make significant changes? Right now, I think MFI has a lot of good things going for it. I only support this acquisition if MFI continues to operate under its current business model. Then, after gaining some experience, we can consider applying some of the same elements to CFL's operations.

Phillip: I prefer to give Gino a year to operate without too much involvement and then CFL can slowly take over the locations and change them to CFL's format. I think that his group training sessions using the machines is only a fad that is likely to die out next year. I also think that the interest in Mudder races will wane and people will once again be looking for the more traditional tried-and-true gyms, like we have.

Rosa: I just wanted to add that we will have to think about how we might want to account for this acquisition and the tax implications of this acquisition on MFI. Let's have SCG give us some guidance on these issues.

Phillip: Well let's move on. I think everyone has had a say. You have an idea to present, Brian?

Brian: I am really excited about this idea because of my love of climbing. I have done a lot of research and found that there is a growing demand for indoor climbing and bouldering wall facilities. In discussions with my climbing friends, there appears to be a real need for these facilities. I examined all our existing locations to see which ones were performing poorly, with low and declining members, and identified eight locations that are not doing well but are the perfect space to build a climbing wall. They are all in old warehouses with really high ceilings. In addition, I could not find any local competitors that currently have indoor climbing facilities, so we could have first mover advantage in these locations. I have prepared some preliminary estimates for the proposal (Appendix VI). It takes a few months to get the walls built, so I would expect that we could be fully operational later in 2022, and certainly by 2023.

Rosa: Brian asked me to look at these forecasts, and they seem reasonable.

Frank: I have seen these climbing walls at some of the trade shows that I have been to, and they are amazing. You can have almost anything you want. But they are very expensive, and I know that you need enough square footage of climbing and bouldering walls to make it interesting for all levels. For this amount of capital investment, can we offer enough climbing walls that will provide plenty of challenge and variety? I would have thought we might have to have spend twice as much.

Brian: I did work with a supplier on this, and they felt that my cost estimates were reasonable and that the proposed size of the climbing facilities would be a good start. There is room to increase it or change it down the road if we want, as we won't initially be using all of the available space. But this will get us started and allow us to test how successful it can be, given we already have the proper space. And with my knowledge of rock climbing, I will work with the supplier to design the routes so that there is a lot of variety and challenges, since I know exactly what climbers will be looking for. I also have a lot of connections to help with marketing and provide advice, as needed.

Phillip: I am not sure we should dramatically change like this. What happens when we start to close gyms to our members? Our brand name will be ruined. We will also likely start to lose members from the other facilities that might not renew on the possibility that we could close their location also. Our name was built on general fitness, not on rock climbing, of which most of us know nothing about.

Rosa: We could cross-market these facilities. We could give discounts to our current members who might be looking for fitness alternatives. I know that climbing is often used for cross-training because it is fun and a complex physical activity, and is often done in pairs or as a group activity.

Sandra: But we know nothing about climbing, as Phillip says. We will have to learn how to market and promote to children and youth, who are the primary users of these facilities. I am also concerned with the approximately 7,100 members at these eight locations who still have time left on their memberships but won't be able to work out once the renovations begin. We will have to compensate them in some way and no doubt this will give us negative press.

Frank: I would rather take this capital and invest in new cardio and weight equipment, and renovate some of our current locations. What about the high insurance premiums that must be paid? There is a lot more risk that a serious accident could happen, and we could end up being sued for this. I am hesitant to support this investment.

Brian: We can have waivers that are signed by each participant, to help protect us. This proposal will give us a completely different revenue stream that targets a new customer in a niche segment within the fitness industry that is not yet as price sensitive as traditional gym memberships. And for the members, I think that many of the current members will just transfer to our other gyms. If we provide incentives, I do not think we will lose as much as forecasted. We have forecasted a worst-case scenario where all members in these locations are lost.

Phillip: Climbing is a fad and will be gone within a few years, well before your nine-year project life. And then what do we do with the facilities?

Sandra: I think that there will be a lot more training and screening of the staff required. We will need individuals that are good with children and can instruct on climbing technique. That also means we will have to terminate our current employees that work at these eight locations.

Phillip: Next? Frank, you have an idea you want to share with the group.

Frank: Yes, I have a proposal that will allow CFL to tap into an increasing market, with little upfront capital. It is consistent with our value to help people achieve their fitness goals. Zenfit Equipment Co. (Zenfit), my old employer, has asked if we would be interested in being a distributor for its equipment in Western Canada. They have provided a draft distributor's agreement, which I am very familiar with, since I used to work as one of their distributors. As you know, CFL currently buys a lot of its cardio equipment from Zenfit since they manufacture reliable and innovative equipment. But there is an even more interesting part to this association, as they want us to help create their group fitness class videos using their new Zentracker machines, which I have provided more detail on (Appendix VII and VIII).

Brian: I have read about these machines. They are seen to be the up-and-coming fitness equipment that takes cross-training to a new level. They are also each fitted with a great TV that allows for streaming of videos. Impressive! I think we should be involved, to be at the leading edge of this growing market.

Frank: Yes, Zenfit is very excited about this and they want to have us demo these machines in some of our facilities. They also want us to run a group fitness class at one of our facilities using these machines. I am thinking that we could convert one spinning room to a Zentracker room to begin with.

Rosa: I have read the distributor's agreement and what I don't like is that we have to achieve the $1 million of equipment sales target quarterly. This is really aggressive, given all of the other known competitors in the industry.

Frank: Yes, it is, but I think it is achievable given what I know about the company and this new machine. I think it's worth a try.

Phillip: We only currently purchase about 40% of our cardio equipment from Zenfit and the other 60% comes from other well-known brands. This agreement will require us to purchase only from Zenfit if they have the machines that we need — which I think would be around 90% of our current cardio equipment expenditures. I don't want someone else to tell me what to buy and controlling these decisions.

Frank: Your numbers are correct, but I think you will find that Zenfit, which has been outspending competitors in the area of R&D, will very often have the better machines on the market.

Brian: I like this idea. It would be great, from a marketing perspective, to create these videos, and give us greater exposure even in our local communities. I think we could draw new members who would want to be part of this online community and be part of our classes. I see us expanding these classes to our other facilities. It will definitely promote some excitement around our brand, which has been lost in recent years.

Sandra: I have watched videos of competitors' fitness streaming, and it is all dependent on the fitness instructor. These video stars must not only be good instructors, but they must also be charismatic, motivational, and entertaining. This is quite a combination of skills and I am not sure who we would get. Without the right instructors, we would not be able to even get 10% of the viewership that has been assumed.

Rosa: To meet our sales targets, we will likely have to sell Zenfit equipment to other gyms that are our competitors.

Phillip: What happens if the Zentracker is a bust — it doesn't work or fails to live up to expectations? We will be blamed for selling these machines and tying our name to it, which will impact negatively on our brand.

Frank: I think this is a great way to slowly move into a new market and get away from being in a rut of only running a traditional gym.

Phillip: I am not convinced, but your opinion is noted. Rosa, you have a final idea.

Rosa: Yes. Amanda, a long-time member, has approached me with an idea to open PurCafés, a healthy food café, in five of CFL's locations. Her proposal looks interesting since she would prepare all the food off site and be responsible for its quality. All we really have to do is renovate the areas and provide the staff (Appendix IX). I will ask SCG to prepare some break-even analysis, but I think the number of customers required will be low and achievable. I think it is a very low-risk way to provide another service to our members.

Brian: I like the idea. This will build a sense of community, and we can advertise to promote the café on our website and social media.

Frank: I also like the idea. It will give us access to people that might not ordinarily come into the facilities. We could do some interesting renovations that would provide an inviting and trendy atmosphere.

Rosa: Amanda has done extensive research into the gym-café market and also has some wonderful ideas on what the café space should look like. CFL would be getting her expertise in this area. Her upscale restaurants are wonderfully decorated.

Phillip: I don't like the idea. I don't want to be dependent on Amanda for the quality of the food and the atmosphere of the café. And our members have never suggested they wanted food and beverages, so why should we spend money on this?

Rosa: No one has ever asked because it has never been suggested. I did an informal survey at the suggested locations and members really liked the idea. Apparently, many of them go off site somewhere, and felt that an on-site café would be well received.

Sandra: I don't like the idea. This will make some of the gyms different based on local needs, and I thought an important differentiator for us was consistency, in that each of our facilities will be same.

Frank: I think it is important to have local differences between the gyms. Amanda has chosen these locations carefully and I have to agree with her suggestions. Currently, there is no local competition, and the fact that the street fronts can be easily renovated is a plus. If it is successful, I think there are at least another eight possible locations that would also work. I think there is little risk with this, so let's give it a try.

Brian: This space would also allow us to host parties and other gatherings to build a community spirit. We could charge extra for these parties, giving us another source of revenues and profits.

Phillip: This suggestion does not help us grow in members or locations, and therefore I think the money spent is a waste.

Rosa: But it will help us differentiate and maybe attract more potential members. We have to do something to stop the steady decline of current members. Showing that we are willing to invest in existing gyms will result in retaining members. It is cheaper to try to retain existing members than to try to get new members all the time, and therefore is a better use of our cash flow.

Frank: I agree. We already have the locations and the members — let's try to keep them rather than adding more locations just for the sake of being bigger. We are already struggling to manage our current size.

Rosa: I also think we should have SCG do some additional industry research into cafés at gyms, and I have made a list of websites (Appendix IX) that might be helpful. One other point is that in my discussions with Amanda, she proposed that this could possibly be a joint arrangement.

Phillip: We need to decide how we will finance any of our strategic decisions. There are two options, as we noted in an earlier meeting. One alternative is a sale and leaseback of our current head office. As you know, the market value of the building has increased, and this might be a way to get some of the cash out. A second source is JAG Trust Bank, a mezzanine bank. I have a friend who works there as a loan manager and he has prepared a proposal (Appendix IV). I think we should have SCG assess these proposals and also determine any accounting or tax implications.

Rosa: Agreed. We should also have SCG provide a discussion of any accounting or tax implications related to any of the strategic initiatives we are asking them to assess.

Sandra: Yes. As well, with all these potential changes, we really need to ensure our performance management system is robust enough. Let's ask SCG for advice on how to improve our performance measurement tools and to provide a framework we could use for performance management and the key metrics that should be tracked.

Phillip: Great ideas. On that note, there are also two staff issues that have become quite serious. The first issue is that I have been hearing rumours that there is a group of personal trainers in a number of our facilities who are selling supplements to their clients and receiving commissions from the suppliers. As you know, we have always had a well-known policy where CFL does not endorse the sale or use of any of these products. Based on my investigation, these particular supplements have not been tested and have questionable results, and the trainers might be falsely marketing them to their clients. None of our trainers have any experience or certification in dealing with supplements. A few clients have let me know that trainers have provided advice and recommendations on which supplements should be purchased. I have not acted on this, but many of these trainers have worked for CFL for a long time and are some of our best-rated trainers. From what I have been able to discover, there are 10 trainers involved.

Rosa: This is really serious, since we could be held liable for this.

Brian: And if this gets out, our reputation is destroyed. I think we need some guidance on what we should do about this; hopefully, SCG can help us with this.

Phillip: On the second issue, Sandra, I think you have some information?

Sandra: Yes. This won't come as a surprise, but there is a group of fitness instructors that are threatening to organize a union if they are not paid fair wages. Currently, they feel they are not being paid for all the hours worked. As you know, I have been bringing this issue to the meetings for the past year and we have kept putting off dealing with it, assuming it would just go away. Instead, it has gotten worse. They are also looking to file a lawsuit to get CFL to pay them for what they work, based on the success of similar lawsuits in the fitness industry.

Rosa: I think they have a valid concern. Currently, we only pay our fitness instructors for the duration of the fitness class. However, the practice has been to have them arrive at the gym at least 15 minutes before class to prepare and mingle with members, and to stay 30 minutes after class to clean up and mingle with members. They also spend time preparing the class itself and they are not compensated for this time. None of this extra time is formally required in our current policies.

Brian: I also see that comments about CFL being an unfair employer are trending on social media. If we don't do something about this, it is going to start impacting our membership.

Phillip: Let's ask SCG to provide some advice on this. If there is nothing else, we are adjourned then.

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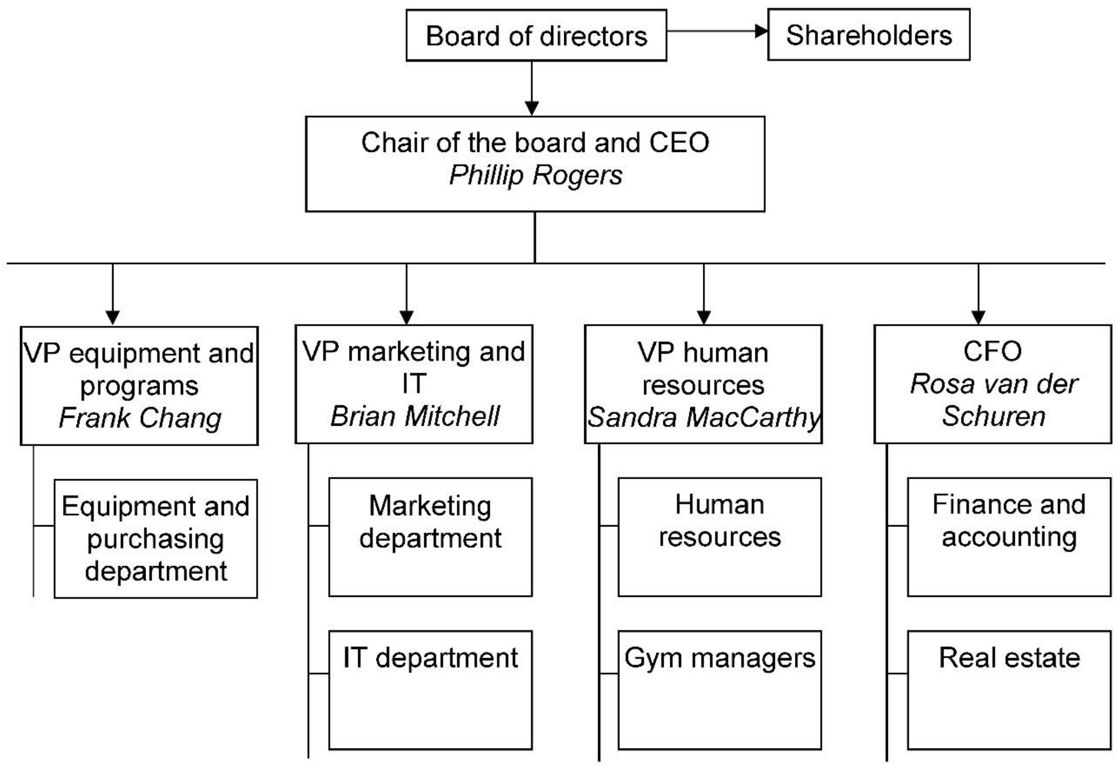
Appendix I
Organizational chart
Prepared by Sandra MacCarthy



Appendix II
CFL financial statements
Prepared by Rosa van der Schuren

CanDo Fitness Limited
Income statement
for the years ended December 31
(under ASPE)
(in C$'000s)

	AUDITED 2021	AUDITED 2020	AUDITED 2019
Revenue	46,200	48,160	50,059
Expenses			
Purchases	1,432	1,493	1,628
Wages	19,065	18,589	19,029
Marketing and advertising	2,480	2,380	2,450
Occupancy costs	6,907	6,876	6,882
Amortization	5,095	4,890	4,326
General and administrative	8,535	8,930	8,923
Total expenses	43,514	43,158	43,238
Operating income	2,686	5,002	6,821
Interest expense	(1,586)	(1,736)	(1,886)
Income before taxes	1,100	3,266	4,935
Income taxes	(276)	(742)	(1,194)
Net earnings	824	2,524	3,741

Appendix II (continued)
CFL financial statements
Prepared by Rosa van der Schuren

CanDo Fitness Limited
Statement of retained earnings
for the years ended December 31
(under ASPE)
(in C$'000s)

	AUDITED 2021	**AUDITED 2020**	**AUDITED 2019**
Balance — beginning of year	11,181	10,657	8,916
Net earnings	824	2,524	3,741
Dividends	(2,000)	(2,000)	(2,000)
Balance — end of year	10,005	11,181	10,657

Property, plant, and equipment			
Opening balance	42,643	41,613	41,322
Capital additions	4,162	5,920	4,617
Amortization	(5,095)	(4,890)	(4,326)
Closing balance	41,710	42,643	41,613

Appendix II (continued)
CFL financial statements
Prepared by Rosa van der Schuren

CanDo Fitness Limited
Balance sheet
as at December 31
(under ASPE)
(in C$'000s)

	AUDITED 2021	**AUDITED 2020**	**AUDITED 2019**
Assets			
Current assets			
Cash and cash equivalents	430	3,069	5,600
Prepaid supplies and expenses	690	760	820
Total current assets	1,120	3,829	6,420
Property, plant, and equipment — net	41,710	42,643	41,613
Total assets	42,830	46,472	48,033
Liabilities			
Current liabilities			
Trade payables and accrued liabilities	4,339	4,306	3,858
Income taxes payable	6	5	38
Current portion — mortgage payable	2,500	2,500	2,500
Total current liabilities	6,845	6,811	6,396
Long-term debt — mortgage payable	22,680	25,180	27,680
Total liabilities	29,525	31,991	34,076
Shareholders' equity			
Share capital — Class A multi-voting common shares (1,000 shares outstanding)	500	500	500
Share capital — Class B common shares (4,000 shares outstanding)	2,800	2,800	2,800
Retained earnings	10,005	11,181	10,657
Total shareholders' equity	13,305	14,481	13,957
Total liabilities and shareholders' equity	42,830	46,472	48,033

Appendix II (continued)
CFL financial statements
Prepared by Rosa van der Schuren

CanDo Fitness Limited
Cash flow statement
for the years ended December 31
(under ASPE)
(in C$'000s)

	AUDITED 2021	**AUDITED 2020**
Operating activities		
Net profit	824	2,524
Amortization	5,095	4,890
Change in working capital balances		
Prepaid supplies and expenses	70	60
Trade payables and accrued liabilities	33	448
Income taxes payable	1	(33)
Total cash flow from operating activities	6,023	7,889
Investing activities		
Investment in property, plant, and equipment	(4,162)	(5,920)
Financing activities		
Repayment mortgage payable	(2,500)	(2,500)
Dividends paid	(2,000)	(2,000)
Total cash flow from financing activities	(4,500)	(4,500)
Change in cash	(2,639)	(2,531)
Opening cash and cash equivalents	3,069	5,600
Closing cash and cash equivalents	430	3,069

Appendix III
Industry benchmarks
Prepared by Rosa van der Schuren

Industry benchmarks	Industry average
Quick ratio	1.7
EBITDA-to-interest ratio	6.0
Current ratio	1.9
Total-debt-to-equity ratio	2.0
Total-debt-to-assets ratio	0.7
Return on equity	20.0%
Operating margin	12.0%
Profit margin	6.0%
Wages as a percentage of revenue	37.0%
Marketing as a percentage of revenue	2.9%
Member churn rate	50.0%

Appendix IV
Financing alternatives
Prepared by Phillip Rogers

Potential sale-leaseback of the head office land and building

Hume Properties REIT (HPR) has offered to buy the land and building currently owned by CFL and lease it back. HPR has offered $8,500,000 (land is $980,000 and the building is $7,520,000) for the total ownership of land and building. Recent appraisals have valued the property between $8,000,000 and $9,000,000. CFL's tax rate on business income is 26%.

The current net book value (NBV) of the land and building:

- land: NBV and original cost of $950,000
- building: NBV of $5,830,000; original cost of $7,500,000; undepreciated capital cost of $5,410,400

Once the sale is complete, HPR will immediately lease back the property to CFL with the following lease terms:

- The lease will be for 10 years, with new terms and conditions renegotiated for any renewal lease. There is no guaranteed residual value.
- The monthly lease payment, due at the beginning of the month for the next 10 years, will be $51,200 per month. The annual borrowing rate implied in the lease is 6% compounded monthly.
- The lease will be triple net, whereby CFL will be responsible for all maintenance and repairs, insurance, and property taxes.

JAG Trust Bank, a mezzanine financing bank

JAG Trust Bank (JAG) has offered to lend up to $3,500,000 to CFL. The loan will be secured by a second lien against the furniture, fixtures, and equipment, and the personal guarantees of the shareholders. In addition, the shareholders will not be able to receive any dividends until the loan is fully repaid. The loan bears interest at an annual rate of 6%, payable monthly. The total amount of the principal is due in five years from the date the loan proceeds are advanced.

Appendix V
Acquisition of Mighty Fitness Inc.
Prepared by Phillip Rogers

MFI is owned solely by Gino Rossi, who founded the company in 2003. MFI has 35 locations in Ontario and Nova Scotia, with a total of 42,000 members, of which 79% are between the ages of 25 to 35. It has an overall churn rate of 20%. Each fitness facility has workout rooms and state-of-the-art cardio and weight-training equipment that is on average only two years old. The facilities range in size from 13,000 to 15,000 square feet.

MFI's philosophy is based on providing functional training equipment where users can get high-intensity interval training (HIIT) workouts. Although it provides small group workout classes, these are all done using the equipment, such as treadmill or elliptical classes, or circuit training. Gino believes that using the equipment allows for a better overall workout and more variety than traditional aerobic classes. Programs are adapted based on local needs, and products and services are not exactly the same across all facilities.

The company's philosophy is to blend fitness with entertainment. Gino believes that it is really important to have staff that are extremely energetic and motivated but that also can motivate members. He sees each facility as a big family. Entertainment is not only in the colourful and upbeat surroundings but also in the music. Each gym has a monthly party for all its members, which allows members to feel like they are part of a community. The company also has inter-facility competitions. All of this inspires a fervent following from its members.

There are four levels of membership, which start at $10 per month and go up to $30 per month, as follows:

Basic $10 per month	**Mighty** $20 per month	**Mighty Plus** $25 per month	**Supreme** $30 per month
• Locker room with showers • Mighty half-hour circuit training • Mighty's online nutrition guidance	• Everything included with Basic • Mighty live online workouts	• Everything included with Mighty • Guest privileges	• Everything included with Mighty Plus • Group fitness classes

Each new member receives an MFI gym bag and MFI T-shirt. Each year, the company has a competition for the design of next year's T-shirt. The member who wins the design competition gets free membership for the year. This has been very successful and has resulted in enhancing the community spirit of the facilities.

Appendix V (continued)
Acquisition of Mighty Fitness Inc.
Prepared by Phillip Rogers

In addition to the membership fees, revenue is earned from the sale of group fitness class passes (for members who do not have the Supreme pass), personal training hours, and admissions to parties and competitions. The company also sells its branded merchandise, which includes T-shirts, other workout clothes, water bottles, and snack bars. The company also runs targeted training programs for specific competitions such as Mudder races, which MFI members will often enter as a team. There is an extra charge for these training programs. The company does not give away free passes, except the guest passes that existing members have as part of their membership.

Included in MFI's other revenue is a one-time gain on disposal of equipment for $400,000. MFI has never paid any dividends, and Gino is paid an annual salary of $100,000. Gino has personally designed all the MFI online videos for training and nutritional guidance, which results in lower IT costs for the company. If MFI hired people to perform this work, the annual market salaries for comparable work would be $450,000 in total, including all benefits. In addition, during 2021, MFI incurred consultants' fees of $100,000 to prepare a strategic analysis for Gino.

MFI's managers and head office staff are the only full-time employees. The fitness instructors and personal trainers are all independent contractors that are paid a set fee depending on the hours worked. These contractors do not have non-compete clauses in their contracts. They are free to work outside the company and have their own clients at other locations. Since they like to work at MFI, there has never been an issue about getting the trainers to put in the hours requested. This system has allowed the company to have overall lower wages and contractor fees.

Gino is offering to sell 50% ownership in MFI for $12 million. The long-term debt, which currently has an interest rate of 8%, is coming due in October 2022. Gino is concerned about renewing this debt and hopes that CFL will agree to guarantee this debt to ensure that favourable rates and terms can be maintained. Gino also notes that MFI has some tax loss carryforwards still available that arose in previous years. For this reason, MFI has not paid income taxes for the past few years. MFI's tax rate is 26%.

Rosa has looked at some of the preliminary information and has estimated that CFL could save at least $300,000 after-tax per year on overhead costs with this acquisition.

Appendix V (continued)
Acquisition of Mighty Fitness Inc.
Prepared by Phillip Rogers

The following is summarized information on recent sales in the industry:

Date of transaction	Company name	Information	Total firm value/ EBITDA	Total firm value/ revenue
July 2020	Solar Fitness Limited	70 locations across Canada Revenue of $124 million; multiple sources of revenue Cardio and weight-training equipment; pools; squash courts Annual memberships of $470	8.4 ×	1.1 ×
August 2020	Judy's Studios Inc.	30 locations in Ontario only Revenue of $20 million; multiple sources of revenue Yoga and meditation studios High-end boutique facilities with annual memberships starting at $700	6.5 ×	0.8 ×
February 2021	KA Fitness Clubs Inc.	250 locations across Canada and Eastern U.S. Revenue of $480 million; multiple sources of revenue Cardio and weight training; yoga; party rooms; corporate locations Monthly memberships of $35	7.5 ×	1.0 ×

Appendix V (continued)
Acquisition of Mighty Fitness Inc.
Prepared by Phillip Rogers

Date of transaction	Company name	Information	Total firm value/ EBITDA	Total firm value/ revenue
March 2021	RJ's Health Clubs Limited	25 locations in Eastern Canada Revenue of $22 million Cardio and weight training; group fitness classes; personal training Annual memberships of $650	6.7 ×	0.9 ×
August 2021	Inspire Life Fitness and Spa Limited	30 locations in B.C. and Ontario Revenue of $35 million, including spa and fitness High end; annual memberships starting at $1,200	8.5 ×	1.8 ×
March 2022	Starre Fitness Limited	45 locations across Canada Revenue of $60 million; multiple sources of revenue Cardio; weight training; fitness classes; skating rinks; nutritional counselling Monthly memberships starting at $45	6.1 ×	1.3 ×

Appendix V (continued)
Acquisition of Mighty Fitness Inc.
Prepared by Phillip Rogers

Mighty Fitness Inc.
Income statement
for the year ended December 31
(under ASPE)
(in C$'000s)

	AUDITED 2021
Revenue	
Membership fees	11,900
Personal training	17,800
Other	15,400
Total revenue	45,100
Expenses	
Purchases	4,010
Wages and contractor costs	15,090
Marketing and advertising	3,500
Occupancy costs	7,500
Amortization	6,200
General and administrative	4,890
Total expenses	41,190
Operating income	3,910
Interest expense — line of credit	(135)
Interest expense — Bank of Brunswick	(3,166)
Income before taxes	609
Income taxes	—
Net earnings	609

Appendix V (continued)
Acquisition of Mighty Fitness Inc.
Prepared by Phillip Rogers

Mighty Fitness Inc.
Balance sheet
as at December 31
(under ASPE)
(in C$'000s)

	AUDITED 2021
Assets	
Current assets	
Cash and cash equivalents	80
Inventories	2,450
Prepaid expenses	180
Total current assets	2,710
Property, plant, and equipment — net	52,700
Total assets	55,410
Liabilities	
Current liabilities	
Line of credit	2,790
Trade payables and accrued liabilities	7,540
Current portion — Bank of Brunswick	4,000
Total current liabilities	14,330
Long-term debt — Bank of Brunswick	33,580
Total liabilities	47,910
Shareholders' equity	
Share capital — 100,000 common shares outstanding	100
Retained earnings	7,400
Total shareholders' equity	7,500
Total liabilities and shareholders' equity	55,410

Appendix VI
Indoor climbing and bouldering wall proposal
Prepared by Brian Mitchell

CFL will convert eight existing locations to indoor climbing and bouldering wall facilities, with each facility having 12,000 square feet of climbing and bouldering walls.

The cost of the walls, other equipment, and renovations required for each facility will be $700,000. These capital assets will qualify for 20% declining balance and the accelerated investment incentive for capital cost allowance (CCA) purposes. The useful life of the assets will be nine years, and they can be sold for salvage equal to $800,000 in total.

The existing cardio and weight equipment at these eight locations can be sold for a total of $320,000.

In addition, there will be an initial investment in prepaid supplies of $400,000. An additional $80,000 will be invested in 2025 and another $80,000 in 2028.

Estimates of membership numbers for each year are as follows:

	2023	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**
Number of climbing members	3,200	3,400	3,600	4,000	4,500	5,000	5,500	6,000	6,000
Annual climbing membership fee	$650	$650	$650	$660	$660	$670	$670	$670	$670

Other sources of revenue for the climbing facilities are estimated as follows, as a percentage of the membership revenues, for the year:

Day passes	90%
Special events	52%
Other	58%

Appendix VI (continued)
Indoor climbing and bouldering wall proposal
Prepared by Brian Mitchell

Direct expenses as a percentage of total revenues are estimated to be:

Wages	21%
Purchases	7%
Marketing	3%
Other expenses (which include general and administration and insurance)	15%

Lost revenue (membership and personal training) from closing the existing facilities at the eight locations is detailed below (in $'000s). It is expected that many members will transfer to other locations, but this has not been factored into the numbers below. Direct costs for the existing gyms are 47% of revenues.

	2023	2024	2025	2026	2027	2028	2029	2030	2031
Revenue	4,800	4,500	4,300	4,000	4,000	4,000	4,000	4,000	4,000

During 2022, the eight facilities will be closed for three months, and lost revenue is expected to be $1,200,000 for this period.

A tax rate of 26% should be used in this analysis, and the cost of capital for this project is 12%.

Appendix VII
Zenfit Equipment Co. proposal
Prepared by Frank Chang

Zenfit, a U.S.-based company, is an equipment supplier, selling traditional cardio equipment and a new line of state-of-the-art cross-trainers, called Zentrackers, that can be custom designed by the customer to add components as required to meet their specific needs. The Zentracker has streaming capabilities for workout videos and live classes.

Zenfit recently lost its distributor in Western Canada and would like CFL to become its exclusive distributor. CFL would have demo equipment available, and trained staff would be available to demonstrate this equipment. Potential customers could come in and try out the different lines of fitness equipment to make their decision about the right type of machine. More importantly, customers could try the Zentracker and determine the components that are right for their needs, prior to purchasing. CFL would sell to customers who want in-home gym equipment; other facilities like hospitals, hotels, and corporate clients; and other gyms.

Zenfit has agreed that CFL would have the exclusive distribution rights for Western Canada, which includes B.C., Alberta, Manitoba, and Saskatchewan. It has also agreed to offer CFL the Eastern Canada region in the future, if this agreement works out. Zenfit stated that in approximately four years, it might be looking for a new Eastern Canada distributor.

Zenfit is a well-known company in the fitness equipment supplier industry. It has been selling equipment for more than 20 years and has always been at the leading edge of the industry. The Zentracker was awarded the prize as the best cross-trainer in the market in 2021, and analysts believe that it will set a new trend in cardio equipment. Zenfit has already seen a large increase in demand for this new and innovative product.

The draft proposed distributor agreement with Zenfit is provided in Appendix VIII. Direct costs related to earning the distributor's fees are estimated to be $50,000 annually.

In addition to being a distributor, Zenfit would like to hire CFL to livestream classes and create workout videos using Zentrackers. These would be made available, along with other instructors' videos, to Zentracker customers that have paid monthly subscription fees to view these videos. Zenfit would like CFL to initially convert one of its spinning rooms to a Zentracker room and provide group classes using these machines. These classes would then be livestreamed and recorded, and the videos made available for later viewing. Zenfit will pay for the recording, which will be done by professionals. Zenfit will pay CFL a flat royalty fee of $0.75 for each video streamed. The target market for these livestreams and videos are predominantly 25- to 40-year-olds.

Appendix VII (continued)
Zenfit Equipment Co. proposal
Prepared by Frank Chang

Zenfit has provided the following assumptions, which it believes are very conservative:

	2022	**2023**	**2024**
Number of Zentracker subscribers	100,000	200,000	350,000
Weekly videos viewed by each subscriber	3	3	3
Percentage that would view CFL's videos	10%	10%	10%

CFL will have to immediately convert one spinning room in one of its locations to a Zentracker room. This will cost $400,000 for new equipment, renovations, and the required technology and cameras to livestream. If it is successful and members are interested, CFL would be able to expand this to some of its other facilities. CCA on the long-lived assets involved is assumed to equal depreciation. A tax rate of 26% should be used in this analysis.

The Zenfit proposal includes both the equipment distribution and video services. Zenfit is not open to pursuing either option separately. The terms of the distributor agreement are also not negotiable.

Appendix VIII
Extracts from draft distributor agreement with Zenfit Equipment Co.
Provided by Frank Chang

EXCLUSIVE DISTRIBUTOR AGREEMENT

This Exclusive Distributor Agreement (“Agreement”) is made and effective on this, the 1st day of July, 2022, by and between Zenfit Equipment Co, Inc., a U.S. Corporation with its principal place of business at 120 Hammond Road, Portland, Oregon, United States, (“Company”) and CanDo Fitness Limited., a Canadian corporation having offices at 589 Southam St., Vancouver, British Columbia, Canada (“Distributor”).

1. Appointment

Company hereby appoints Distributor as its exclusive Distributor for the Products in the exclusive Territory of Western Canada, including British Columbia, Alberta, Manitoba, and Saskatchewan. Distributor’s sole authority shall be to solicit orders for the Products in the Territory in accordance with the terms of this Agreement. “Products” includes all the Company’s Fitness Equipment Products that are available for sale.

3. General Duties

Distributor shall use its best efforts to promote the Products and maximize the sale of the Products in the Territory. Distributor will provide adequate space and time for the demonstration of Products to potential customers and Distributor will work with the customer to determine the best choice of equipment. Monthly, the Company shall provide Distributor with the Product Sales Report showing customer name, Products ordered, and date of sale. All sales will be made directly between the Company and the Customer.

5. Conflict of Interest

Distributor warrants to Company that it does not currently represent or promote any lines or products that compete with the Products. During the term of this Agreement, Distributor shall not represent, promote, or otherwise try to sell within the Territory any lines or products that, in Company’s judgment, compete with the Products covered by this Agreement. Distributor shall provide Company with a list of the companies and products that it currently uses in its facilities and shall notify Company in writing of any new companies and products at such time as its promotion of those new companies and products commences.

6. Independent Contractor

Distributor is an independent contractor.

Appendix VIII (continued)
Extracts from draft distributor agreement with Zenfit Equipment Co.
Provided by Frank Chang

7. Distributor’s Purchases for Own Use

Distributor has the right to purchase Products for its own use at a discounted price of 10% off the normal retail price. This Agreement requires Distributor to purchase cardio equipment only from Company if they have the machines that are needed. In cases where Company does not produce the type of cardio equipment required, then another supplier may be used, on approval by Company.

12. Demo Product

Company will provide Distributor, for free, all demo Products that Company wants shown and available for demonstration. These Products will become the property of Distributor. Distributor shall have full responsibility of keeping each demo Product in proper operating condition during the entire length of the contract.

13. Additional Responsibilities of Distributor

A. Expense of doing business: Distributor shall bear the entire cost and expense of conducting its business in accordance with the terms of this Agreement.

B. Facilities: Distributor shall provide itself with, and be solely responsible for, (1) such facilities, employees, and business organization, and (2) such permits, licences, and other forms of clearance from governmental or regulatory agencies, if any, as are necessary for the conduct of Distributor’s business operations in accordance with this Agreement.

C. Promotion of the Products: Distributor shall, at its own expense, vigorously promote the sale of and stimulate demand for the Products within the Territory by direct solicitation, which will be all expressly authorized by Company.

D. Customer service: Distributor shall diligently assist customers’ personnel in using the Products and shall perform such additional customer service as required to effectively sell the Product and as Company may reasonably request.

16. Term

This Agreement shall commence on the date first written above and shall continue for three (3) years unless terminated earlier as provided herein. Thereafter, this Agreement shall continue until terminated upon at least ninety (90) days notice by Company or ninety (90) days notice by Distributor.

Appendix VIII (continued)
Extracts from draft distributor agreement with Zenfit Equipment Co.
Provided by Frank Chang

The below signed parties hereby acknowledge that they have read and understand the entire Agreement, that they have authority to enter this Agreement on behalf of their respective organizations, and that they have freely and voluntarily executed this Agreement as of the day and year first written above.

Attachment 1: Terms and Conditions of Sale of Products

Shipping and delivery timing: Company shall determine a “ship by” date separately for each order received from Distributor. Company shall be responsible for shipping the order no later than the “ship by” date for each order received and the goods will be shipped directly to the customer. At no time will Distributor take ownership of the goods. The customer will pay the Company directly for all sales.

Minimum quarterly sales to maintain exclusivity: Distributor must sell at least C$1,000,000.00 per calendar quarter to maintain exclusivity. Failure by Distributor to meet this minimum for two consecutive quarters shall subject Distributor to loss of exclusivity and possible termination of this Agreement.

Minimum annual sales to renew exclusivity: If each quarterly sales minimum is met as outlined above (meaning minimum annual sales of C$4,000,000), then Distributor shall be entitled to renewal of its exclusivity under this Agreement for an additional year subject to new quarterly minimums to be determined by Company.

Product prices will range from C$5,000 to C$15,000 per product.

Company agrees to pay Distributor a distributor’s fee of 15% of the retail price of any Products sold. This distributor’s fee will be paid within 30 days of the sales date. Sales made to CFL itself or its affiliates will not earn the distributor’s fee or count toward minimum quarterly and annual sales requirements.

Appendix IX
PurCafés proposal
Prepared by Rosa van der Schuren

Amanda Parska is proposing opening health food restaurants in five CFL locations. Amanda owns a company called PurFood Inc. PurFood owns three thriving high-end vegetarian restaurants that are open only for dinner — two are in Vancouver and one is in Calgary. Amanda would like to open a more casual offshoot of her successful restaurants in CFL's fitness facilities, and she has identified five CFL locations that might work perfectly. These locations are different from the locations suggested for the climbing and bouldering wall facilities. Amanda has selected these facilities based on her analysis of local competition and because they are close to both non-member clientele and to her restaurants, where the food will be prepared. She has also visited each facility, with me, and feels that a street-front restaurant could be built, which would be ideal, as a storefront would allow the restaurant to draw in non-members.

Amanda's concept is for a casual café, called PurCafé, that would sell healthy food and beverages and premium coffee and tea. Each café would serve smoothies, juice, coffee, tea, and light menu options. The café would be open daily from 6:00 a.m. to 3:00 p.m. Currently, these five selected locations have a large front lobby, which could be transformed into a restaurant. CFL would have to move around some of the equipment, but it should be possible, making better use of existing space.

The plan is to use about 1,000 square feet in total per location. There will be a bar and small tables, with comfortable seating for up to 50 people. The costs to renovate the space and for all related equipment per location is as follows:

Leasehold improvements	$250,000
Furniture and fixtures	110,000
Kitchen and dining smallwares	30,000
Total	$390,000

These costs will be amortized over 10 years on a straight-line basis.

Amanda and I are trying to decide between a lower-priced and a higher-priced menu. For the lower-priced menu, the average number of people for breakfast and lunch are as follows:

	Mon.	Tues.	Wed.	Thurs.	Fri.	Sat.	Sun.
Breakfast	75	75	75	75	75	50	50
Lunch	100	100	100	100	100	100	100

Appendix IX (continued)
PurCafés proposal
Prepared by Rosa van der Schuren

It is expected that for the higher-priced menu, there will be 20% fewer people. Amanda expects that 50% of the daily customers will be members at the facility and 50% will be non-members coming in off the street. At these five locations, the average number of members that visit the facilities each day are 200.

Amanda estimates that the average order and variable costs will be as follows:

- Lower-priced menu will be $12 per person for breakfast (smoothies, juices, coffee, tea, and breakfast items) and $20 per person for lunch. The cost of the food and beverage (paid to PurFood) will be 47%.
- Higher-priced menu will be $14 per person for breakfast (smoothies, juices, coffee, tea, and breakfast items) and $24 per person for lunch. The cost of the food and beverage (paid to PurFood) will be 52%.

Additional fixed costs include:

- Labour: Two people to staff the café during open hours, at an hourly rate of $20, including benefits.
- Advertising and marketing costs: Estimated to be $15,000 annually.
- Operating costs: Estimated to be $50,000 annually. These costs include insurance, hydro, repairs and maintenance, and supplies.

As part of this arrangement and to compensate Amanda for managing the cafés, PurFood will be paid 15% of the net operating profits before taxes of the cafés. Amanda mentioned that annually, she would like to obtain a high level of assurance that the net operating profit figure for the past year used for calculating her compensation is appropriate.

For projects of this size, the company expects a payback period of 21 months. As part of this arrangement with Amanda, CFL must agree to renovate a minimum of five different locations for cafés.

During 2022, renovations will start and will be fully completed in all five locations by January 1, 2023.

The following websites can be used for additional research into this industry:

- https://aaronallen.com/blog/canadian-restaurant-industry
- https://afterclass.classpass.com/is-an-in-house-smoothie-bar-worth-the-investment/

Appendix X
Data collection, storage, and analysis
Prepared by Brian Mitchell

When an individual is interested in joining CFL, they must complete a membership application form that includes the following information:

- first name
- last name
- job title
- social insurance number
- street address
- email address
- gender
- credit card type
- credit card number

This information is used to perform a credit check on the applicant. The information is stored in CFL's member management system. Once the credit check has been completed, the application is manually approved by the member services manager, and the member management system automatically generates a unique Member_ID and username.

The Member_ID is used to track the member activities at the gym. Activities are tracked in a separate member engagement database that includes:

- the date of the member's last visit (last_visit)
- the average frequency of the member's visits based on the last 12 months (visit_frequency):
  - daily (5 to 7 times per week)
  - semi-weekly (3 to 4 times per week)
  - biweekly (1 to 2 times per week)
  - monthly (less than 4 times per month)
  - yearly (less than 11 times per year)

Appendix X (continued)
Data collection, storage, and analysis
Prepared by Brian Mitchell

- program enrolment history (class_1; class_2; class_3)
  - barre
  - hot yoga
  - bootcamp
  - kickboxing
  - Pilates
  - spin
  - Zumba

The username gives members access to the members-only section of CFL's website, where they can update their personal information, register for classes and information sessions, and book personal training sessions.

To improve member satisfaction, each member is emailed a customer service survey once per year. The last survey was distributed in November 2021, with responses opened until December 15, 2021.

The latest survey consisted of five standardized questions. Members were asked to rank CFL's performance on a scale of 1 to 5, with 1 being "very poor," 2 being "poor," 3 being "neutral," 4 being "good," and 5 being "very good."

Members were asked to select "NA" if the question is not applicable to them.

The standardized questions (and the database field the responses are stored in) were:

1. How are we doing on cleanliness? (survey_1)
2. How are we doing on maintenance? (survey_2)
3. How are we doing on program delivery? (survey_3)
4. How are we doing on accessibility? (survey_4)
5. How are we doing on cost? (survey_5)

The survey is delivered by a third-party vendor that is given access to CFL's member management system to harvest the email addresses of CFL's members. Survey results are stored on the third party's system and can be accessed for up to three years. It is the responsibility of CFL to download and retain any documentation they want to keep longer than three years.

Appendix X (continued)
Data collection, storage, and analysis
Prepared by Brian Mitchell

Board directive

The board would like to be able to combine a member's personal data, blend it with data on gym and class attendance, and then blend it with the survey results from that member to see if there are any insights to be gained. The board would like to provide better customer service, which should improve customer retention, and assess what classes CFL should be providing at which locations.

Since CFL has 40 locations and 49,800 members, the board has requested that the initial analysis be completed at a single location. If they believe there is value in the results, they will extend data analysis to all its locations. To start, the board has selected the original location in Vancouver.

To complete the analysis, CFL's IT department has provided the relevant data from the member management system (MemberData.xls*), the member engagement system (AttendanceData.xls*), and the most recent survey (SurveyData.xls*).

Member activities are tracked indefinitely, but for the board's purposes, only member activities in the past 12 months have been provided.

Data breach

In late December 2021, a member of CFL's management team at one of its Calgary locations fell victim to an email phishing scheme. The employee clicked on a link in an email that he believed to be from a secure source. This set in motion a series of events that allowed unauthorized parties to gain access to that location's member management system. None of the member data was encrypted, and the unauthorized party was able to access all of the member data.

To prevent further infiltration, CFL's IT department has taken the location offline for the time being and are asking members to call the gym to register for a class or book a personal training session. CFL has not yet notified members of the breach.

In addition to the analysis to be performed on the Vancouver location, the board would also appreciate some assistance understanding how to bring the location back online, how to prevent another attack, and, if necessary, how to communicate the breach to its members.

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* NOT INCLUDED

APPENDIX C

THE COMMON FINAL EXAMINATION
DAY 1 CFL VERSION 1 BOOKLET – SEPTEMBER 7, 2022

COMMON FINAL EXAMINATION
SEPTEMBER 7, 2022 – DAY 1

Case (CFL-Version 1) **(Suggested time: 240 minutes)**

It is July 4, 2025, and your boss at Serringers Consulting Group LLP (SCG) has assigned you to another engagement with CanDo Fitness Ltd. (CFL).

Since SCG's last engagement with CFL in 2022, the number of members at CFL's traditional fitness gyms has continually declined. This is largely due to an increase in competition from new companies that have entered the fitness market, which continues to grow rapidly.

Over the past three years, CFL made two major investment decisions. First, CFL entered into a five-year agreement with Zenfit to become the Western Canadian distributor of Zenfit products and to livestream videos for Zenfit's online exercise platform, Zenfit Live. Second, CFL converted eight of its fitness gyms to climbing facilities. So far, both investments have been successful. CFL declined the option to acquire Mighty Fitness Inc. (MFI), as well as the proposal to develop PurCafés at five of CFL's fitness gyms. At the company's 32 remaining fitness gyms, CFL has maintained its approach of offering the same consistent format at all locations.

CFL successfully resolved the dispute with its fitness instructors by increasing their compensation rates, and now pays them slightly above the industry average. CFL let go the personal trainers who were caught selling supplements. Also, late in 2024, Rosa resigned as a CFL board member and as the company's CFO, and wants to sell her 1,000 Class B common shares in CFL as soon as possible.

To finance the climbing-facility conversions and the ongoing need to purchase new equipment, CFL accepted the sale-leaseback option that Hume Properties REIT (HPR) offered in 2022. As of today, CFL has $2 million of cash available for strategic investment. As most creditors have restricted lending to smaller fitness companies, the company does not have access to any new debt facilities.

The company's mission, vision, and core values have not changed.

CFL's Board of Directors has asked you, CPA, to review the information that has been provided and draft a report that analyzes and makes a recommendation for each proposal that has been presented. The board would also like you to comment on CFL's overall strategic direction, and on how each proposal might affect that direction. For this engagement, please ignore any tax implications within your analysis and recommendations.

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APPENDIX I
BOARD MEETING WITH CPA IN ATTENDANCE

Phillip: Thank you for joining us today, CPA. As you know, our 32 fitness gyms are struggling. Without a major change, I am not sure whether we can keep them open for business.

Brian: In 2021, we had over 50,000 annual members at our fitness gyms. Today, we have closer to 35,000. We lowered the cost of our annual memberships, but that tactic has not worked. When you consider the cost to purchase new equipment each year, our fitness gyms are no longer profitable.

Phillip: Our competitors have invested a lot of money into both new and existing gyms, making it almost impossible for us to compete while remaining profitable. I agree with Brian—the current format of our fitness gyms is no longer working. If we want our fitness gyms to survive, we need to determine how to specialize them. It appears we have two options: target either the under-40 market or the over-55 market.

Sandra: That is right, Phillip. Our market research shows a clear distinction between these two age demographic groups. We can no longer cater to everyone.

Frank: Let's have CPA help us make that decision.

Phillip: Excellent. CPA, an objective for CFL in the coming years is to improve its EBITDA. As you analyze each proposal, please pay particular attention to that figure.

I have compiled select data from our recent member survey, which details the different preferences of our two potential target demographics (Appendix III). As you can see, it would be hard to please both groups within the same gym.

Sandra: Our market research suggests that the under-40 market is growing significantly faster than the older demographic. In fact, the under-40 group has never been so focused on their health and fitness. We could take advantage of this growth by modernizing our gyms with all the latest equipment, which is what the younger demographic clearly wants.

Brian: However, the over-55 group is willing to pay a bit more for a gym membership that suits their preferences. Also, our wage expense would decrease with the over-55 group because this demographic is satisfied with fewer fitness classes relative to the younger group.

APPENDIX I (continued)
BOARD MEETING WITH CPA IN ATTENDANCE

Sandra: That may be true, but more of our current members are in the under-40 group. A switch in our focus to the over-55 group would be a significant change to our fitness gyms. If we focus on the older demographic, many of our current members would be pushed away.

Another reason to focus on the under-40 market is CFL's current synergy with Zenfit. Our agreement with Zenfit has worked well, and our Zenfit product sales are highest with the under-40 demographic. And we now have the opportunity to become Zenfit's exclusive national distributor in Canada.

Frank: I think we should be careful, Sandra. I reviewed our original projection for Zenfit sales and it may be overly optimistic (Appendix V). In the first six months of this year, we have seen a 20% drop in unit sales from the same period in 2024, and because of increased competition for streaming fitness videos, we also project the number of Zenfit Live subscribers will drop by 10% annually when compared to 2024. As it currently stands, I expect these trends to continue.

Sandra: That is something to consider. However, Zenfit just announced the launch of a new Zentracker machine for next year. It is technologically advanced, integrates well with almost all wearable fitness devices, and has received great reviews by early users. This upgraded machine should help boost Zenfit sales.

Brian: Becoming the national distributor of Zenfit products would help CFL's brand gain more exposure and would not require an upfront cash investment. However, there are many other new fitness machines that are expected to enter the market in the next few months and years, and many of these machines have impressive built-in technology.

Sandra: That's right, Brian. Zenfit also mentioned that, if we do not agree to extend our contract now and become their national distributor, Zenfit will not renew our contract when it expires in two years. They already have several companies interested in becoming their national distributor, one of which has offered CFL $9 million to buy our current distributor and video production rights.

Brian: Next, I have identified six suitable locations where CFL could open new climbing facilities. So far, the performance of our existing eight climbing facilities has surpassed expectations. One reason for this success is the growing popularity of climbing, which is expected to continue to grow for the foreseeable future.

APPENDIX I (continued)
BOARD MEETING WITH CPA IN ATTENDANCE

Frank: Another big reason for their success has been your contribution, Brian. Your climbing expertise has been a big advantage for us, and our members are very satisfied with the climbing facilities. Across all age demographics, our membership numbers at the climbing facilities continue to increase each year. As such, we do not need to specialize this aspect of our business for any particular age demographic.

Brian: Thanks, Frank. If we open new climbing facilities, I am confident that they will be even more successful, as we have learned a lot from opening our first eight facilities. However, once we have over 10 climbing facilities, we will have to hire a senior manager to assist me, as there is a limit to the number of locations I can effectively manage by myself. But I am not sure that will be necessary; Phillip mentioned to me before the meeting that we received an offer to purchase our climbing facilities.

Phillip: Yes. We received a generous $12 million offer for all eight of our existing climbing facilities. This is something we should seriously consider.

Brian: It would be tough to let the climbing facilities go, especially because we do not have much competition in this area of our business; most new entrants to the industry seem focused on the fitness gym market.

Phillip: Another opportunity we should consider relates to RJ's Health Clubs Limited (RJ). RJ owns 25 gyms in Eastern Canada, which share a very similar format to CFL's current fitness gyms. Unfortunately, the company is going out of business.

Sandra: Why would we want to purchase a company that is going out of business?

Phillip: Good question, Sandra. I am not sure that we do. However, at $7.5 million, the asking price for RJ is very low—it was purchased for almost three times that amount just a few years ago! If we could put RJ back on track, we would significantly expand our fitness gym operations. CFL would then become a national brand.

Frank: Each RJ location has a yoga and meditation studio. This unique feature would help CFL take advantage of the growth in popularity of those two activities.

Sandra: Okay, but RJ is still going out of business. Do we know why it struggled so much?

APPENDIX I (continued)
BOARD MEETING WITH CPA IN ATTENDANCE

Phillip: For the same reason that we are—RJ has lost a significant number of its members to the new competition within the industry. It tried a few tactics to boost sales, such as increasing the number and variety of fitness classes offered, and increasing its marketing, but that only increased costs and had little effect on improving member satisfaction. Like CFL, RJ is currently trying to accommodate members from all age demographics. If we acquire RJ and target a specific age group, I think that the research and analysis we have done for our existing fitness gyms would apply to the RJ locations as well.

Finally, we need to find a replacement for Rosa. In addition to needing a new director, we need to find someone to purchase Rosa's shares of CFL.

Brian: I might have someone. Louisa Rice is a CrossFit competitor who gained a large following on social media after she won last year's world championship. She used to climb competitively, and I have known her for years. She lives in British Columbia and is very interested in becoming a shareholder of CFL. She would use her winnings from the CrossFit championships to buy Rosa's shares. Her following on social media would provide CFL with instant exposure.

Phillip: Besides her social media following, what would Louisa provide as a board member?

Brian: Louisa is a professional athlete and has a passion for teaching. Her knowledge would undoubtedly help CFL create more unique fitness classes, which we could offer in our gyms. I know from experience that Louisa's workouts are always intense!

Frank: I have another potential new shareholder and board member that we should consider. His name is Albert Fong, and he lives in Quebec. We met many years ago when we were both on the professional boxing circuit. Albert sustained a shoulder injury that unfortunately ended his career. Since then, he has had a successful career in corporate finance, but now wishes to return to the fitness world.

Phillip: I like the fact that Louisa is still involved in the fitness world. Given his injury, is Albert still able to be active?

Frank: Yes, but his focus is on less intense exercise. After his injury, Albert became an expert on restorative styles of fitness, such as Pilates and yoga, and is now a certified trainer for both.

Phillip: That is very interesting.

APPENDIX I (continued)
BOARD MEETING WITH CPA IN ATTENDANCE

Phillip: Everyone, thank you so much for coming, and contributing your thoughts today. CPA, as you can see, we have some critical decisions to make. Your analysis and advice on these matters will be greatly appreciated.

CPA: I will start working on my report immediately.

APPENDIX II
INDUSTRY UPDATE

The increasing popularity of fitness among all age demographics has resulted in a large increase in the number of fitness gyms across the country, which has led many fitness companies to lower their annual membership fees in the hope of attracting more members—a trend that is expected to continue. Most of these new gyms are equipped with modern, high-tech equipment.

Wearable fitness devices that integrate with exercise machines have become particularly popular in the last two years. Most wearable fitness devices can connect directly with the new, high-tech exercise machines, to track the users' exercise output and biometric data. As a result, exercise machines that can connect to these devices are in demand; this increased demand has led to the development and release of many new, technologically advanced fitness machines.

Due to the increased number of loan defaults in the past two years among smaller fitness facility operators, lenders have become reluctant to finance gym companies with fewer than 50 locations. Also, recent sales within the industry indicate that fitness and recreation facilities are being sold for an average of six times annual EBITDA.

APPENDIX III
PREFERENCES BY AGE DEMOGRAPHIC
(Prepared by Phillip Rogers)

According to the member survey recently conducted at CFL's 32 fitness gyms, there is a clear distinction between the preferences of two age demographics: those under 40 years old, and those over 55 years old. For the 40-to-55 age demographic, no clear preference patterns were noted other than a slight preference for more modern machines.

	Under 40 Years	**Over 55 Years**
Requested activities	Varied widely, such as free weights, resistance machines, many different kinds of fitness classes, martial arts, climbing, swimming, and diving boards.	Limited to free weights, basic resistance machines, and fitness classes.
Equipment type	Modern, high-tech, able to integrate with fitness apps and wearable fitness devices.	Simple to use, and not constantly changing.
Fitness class instructors	Prefer a variety of classes and instructors with specialized expertise.	Prefer to have the same instructor from class to class.
Fitness class types	High-intensity interval training; specialized classes focusing on either cardio or strength training.	Lower-intensity aerobics and cardio classes, and yoga/meditation classes.
Most important aspect of fitness facility	Variety (of activities, classes, machines, etc.) and technologically-advanced machines.	Consistency of equipment and classes, and community (this group is reluctant to change gyms because of their connection to the gym's community).
Least important aspect of fitness facility	Community.	High-tech equipment.
Typical length of use of the same piece of workout equipment	Less than one year, and sometimes only briefly, such as for one week.	A long time, sometimes for years.
Use of the Zentracker machine by Zenfit	Used, as the equipment is good, but many stopped using it because it does not connect to wearable fitness devices.	Very rarely, as the machines are too complicated.

APPENDIX IV
FITNESS GYMS
(Prepared by Phillip Rogers)

A 12-month earnings report for CFL's 32 fitness gyms, which still operate under the company's "one-size-fits-all" approach, is as follows:

For the year ended December 31, 2024

Number of members by age	
Younger than 40	10,854
40 to 55	16,653
Older than 55	10,030
	37,537
Revenue	
Membership fees	$ 21,396,000
Personal training sessions	13,262,000
Total revenue	34,658,000
Operating expenses	
Purchases	1,191,000
Wages	19,065,000
Marketing and advertising	1,786,000
Occupancy costs	5,691,000
General and administrative	6,691,000
EBITDA	$ 234,000

APPENDIX IV (continued)
FITNESS GYMS
(Prepared by Phillip Rogers)

Option #1 – Modernizing Gyms

If CFL chooses to target the under-40 market, membership forecasts are as follows:

	2026		2027		2028	
Number of members by age						
Younger than 40	16,281	(+50%)	24,422	(+50%)	36,632	(+50%)
40 to 55	18,318	(+10%)	20,150	(+10%)	22,165	(+10%)
Older than 55	2,006	(-80%)	2,006	(0%)	2,006	(0%)

- Annual gym memberships will be priced at $550.
- As more members are expected to use online training applications instead of CFL's personal trainers, revenue from personal training sessions is expected to decline by 10% in each of the next three years.
- Given the need to hire additional fitness class instructors, an initial increase in wages of 5% is expected in 2026, but should remain stable after that.
- Annual equipment investment costs are expected to be $7 million.
- All other expenses are expected to remain the same as in 2024.

Option #2 – Specializing Gyms

If CFL chooses to target the over-55 market, membership forecasts are as follows:

	2026		2027		2028	
Number of members by age						
Younger than 40	2,171	(-80%)	2,171	(0%)	2,171	(0%)
40 to 55	14,988	(-10%)	13,489	(-10%)	12,140	(-10%)
Older than 55	12,036	(+20%)	14,443	(+20%)	17,332	(+20%)

- Annual gym memberships will be priced at $650.
- Given the over-55 age segment's demand for personal trainers, revenue from personal training sessions is expected to increase by 5% in each of the next three years.
- Given this age segment's fitness class preferences, an initial 25% decrease in wages is expected in 2026, but should remain stable after that.
- Annual equipment investment costs are expected to be $1 million.
- Annual marketing expense will increase to $2.5 million.
- All other expenses are expected to remain the same as in 2024.

APPENDIX V
INFORMATION ON ZENFIT PROPOSAL
(Prepared by Sandra MacCarthy)

Actual and projected earnings information from the current Zenfit agreement is as follows:

	Actual			Projected (Note 1)	
	2022	**2023**	**2024**	**2025**	**2026**
Distributor's fee					
Units sold	435	683	546	700	750
Annual sales (Zenfit products)	$ 4,350,000	$ 6,830,000	$ 5,460,000	$ 7,000,000	$ 7,500,000
Distributor's fee (15% of sales)	$ 652,500	$ 1,024,500	$ 819,000	$ 1,050,000	$ 1,125,000
Less related direct costs	$ 76,000	$ 84,350	$ 81,800	$ 50,000	$ 50,000
Annual distributor's fee (net)	$ 576,500	$ 940,150	$ 737,200	$ 1,000,000	$ 1,075,000
Video royalty fees					
Number of subscribers	100,000	225,000	202,500	255,000	350,000
Annual CFL viewed videos	1,560,000	3,510,000	3,159,000	3,978,000	5,460,000
Royalty rate per video viewed	$ 0.75	$ 0.75	$ 0.75	$ 0.75	$ 0.75
Annual video royalties (net)	$ 1,170,000	$ 2,632,500	$ 2,369,250	$ 2,983,500	$ 4,095,000
EBITDA to CFL	$ 1,746,500	$ 3,572,650	$ 3,106,450	$ 3,983,500	$ 5,170,000

Note 1 – These figures were projected by CFL in 2022 before the original Zenfit agreement was signed.

Additional Information:

- The proposed exclusive national distributor contract has a five-year term.
- In order to retain exclusivity over the sale of Zenfit products, CFL must achieve a minimum of $10 million in annual sales as Zenfit's national distributor.
- In addition to the Zenfit showrooms that CFL already has in Western Canada, the proposed contract specifies that CFL must provide at least 10 different showrooms throughout Eastern Canada, so that potential customers can try the equipment prior to purchase.
- The national distributor has the right to purchase Zenfit products for its own use at a discounted price of 15% off the normal retail price.
- With its advanced technology, Zenfit products retail at the high end of the price range of comparable products.
- Zenfit's livestreamed videos are most popular with the 25-to-39 age demographic.

APPENDIX VI
CLIMBING FACILITIES
(Prepared by Brian Mitchell)

Actual earnings information for CFL's eight existing climbing facilities is as follows:

	2023	2024
Number of members	3,500	3,920
Annual membership rate	$ 660	$ 660
Revenue		
Membership fees	$ 2,310,000	$ 2,587,200
Day passes	2,079,000	2,328,480
Special events	1,201,200	1,345,344
Other	1,339,800	1,500,576
Total revenue	6,930,000	7,761,600
Expenses		
Wages	1,455,300	1,629,936
Purchases	485,100	543,312
Marketing	207,900	232,848
Occupancy costs	1,400,000	1,400,000
Other	1,039,500	1,164,240
Amortization	622,222	622,222
Total expenses	5,210,022	5,592,558
Operating income	$ 1,719,978	$ 2,169,042

Additional Information:

- The eight existing climbing facilities were originally fitness gyms that were converted. Because the next six potential locations are not currently CFL locations, it will cost more to prepare and open these locations ($850,000 per location).
- There has been some brand confusion between CFL's fitness gyms and its climbing facilities. When the climbing gyms were initially opened, members of CFL's fitness gyms were angry that their fitness gym membership did not give them access to CFL's climbing facilities.
- CFL received many complaints from the members who lost access to the fitness gyms that were closed in order to be converted into climbing facilities; some cancelled their memberships entirely.
- Since opening, the climbing facilities have had two major injuries. In both cases, the climber was found to have used the equipment improperly, and because the climbers signed a waiver prior to using the facilities, CFL was not held liable.

APPENDIX VII
RJ'S HEALTH CLUBS LIMITED
(Prepared by Phillip Rogers)

RJ provided CFL with the following earnings information from RJ's 25 existing gyms:

	2022	2023	2024
Number of members by age			
Younger than 40	5,524	4,630	3,528
40 to 55	9,354	8,570	7,836
Older than 55	6,980	7,735	8,174
	21,858	20,935	19,538
Revenue			
Membership fees	$ 13,989,120	$ 12,561,000	$ 10,745,900
Personal training sessions	7,367,500	6,630,750	6,344,000
	21,356,620	19,191,750	17,089,900
Operating expenses			
Purchases	929,537	935,038	941,895
Wages	5,719,731	6,672,750	7,054,050
Marketing and advertising	361,587	724,230	1,207,050
Occupancy costs	3,453,500	3,453,500	3,453,500
General and administrative	4,267,625	4,272,250	4,277,021
EBITDA	$ 6,624,640	$ 3,133,982	$ 156,384

Additional Information:

- The number of members within both the under-40 and the 40-to-55 age demographics has been in decline. This is largely due to increased competition from gyms that offer modern facilities with high-tech equipment. Because RJ did not have sufficient cash to purchase modern equipment, its fitness machines have become outdated.
- If CFL agrees to the purchase agreement, all of RJ's current assets, lease agreements (all RJ locations are leased rather than owned), and staff members would be transferred to CFL; however, CFL would not be required to retain any of RJ's current board members.
- RJ has 10 locations in Ontario, 10 in Quebec, and 5 in Atlantic Canada.
- RJ has continually lowered its price for an annual membership, which is currently set at $550.
- RJ members say they are satisfied with the variety of fitness classes offered, but the attendance of individual classes declined as the number of available classes increased.

APPENDIX D

DAY 1 (CFL VERSION 1) – SEPTEMBER 7, 2022
MARKING GUIDE AND SAMPLE CANDIDATE RESPONSE

MARKING GUIDE
CANDO FITNESS LIMITED (CFL)
VERSION 1

Summative Assessment #1 (Situational Analysis)

For Summative Assessment #1, the candidate must be assessed for reasonableness of attempt:

Yes – The candidate used a reasonable situational analysis when analyzing the major issues facing CFL.

Unsure – The candidate attempted to use a reasonable situational analysis when analyzing the major issues facing CFL.

No – The candidate clearly did not use a reasonable situational analysis when analyzing the major issues facing CFL.

Based on the 2020 Competency Map:

Technical Competency
2.3.2 Evaluates the entity's internal and external environment and its impact on strategy development.

Enabling Competencies
1.4.1 Performs work carefully, thoroughly and competently in accordance with relevant technical and professional standards
2.1.1 Applies knowledge of the organization's competitive environment and strategic direction when performing assigned work
2.1.3 Identifies the strategic impact of internal decisions and external influences on project plans and initiatives
6.1.1 Identifies and articulates issues within areas of work responsibility
6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

The candidate is expected to complete an appropriate situational analysis.

The focus should be on describing the factors that have changed since Capstone 1 that will affect the decisions at hand. Recapping parts of the mission/vision and relevant KSFs, and presenting relevant elements of the SWOT, is appropriate.

The candidate should draw upon their situational analysis when analyzing the major issues facing CFL (how to specialize the fitness gyms, sell/expand the Zenfit agreement, sell/expand the climbing facilities, and whether to acquire RJ's Health Clubs).

Mission/Vision

CFL's vision, mission, and core values approved by the Board of Directors in 2017 were:

Vision statement: *"To provide the means to motivate and help adults to achieve their goals."*

Mission statement: *"We are a company dedicated to educating and motivating adults to embrace a fit and healthy lifestyle in a friendly and nonjudgmental atmosphere, providing state-of-the-art equipment and innovative, fun, and challenging group classes. We also strive to further develop health and wellness in the local communities*."

Core values:

1. All employees are caring and understanding of members and work as part of a team to meet the corporate goals and mission. Members, guests, and staff are treated with honesty, dignity, and respect at all times.
2. We continuously update our equipment to ensure that it is leading edge and provide ever-changing group classes that stay up to date with the current trends. We provide unmatched service by having uniquely qualified and passionate staff.
3. All staff are committed to their own fitness goals and healthy living and are able to motivate members to do the same.
4. We strive to build a community of friends in a safe and supportive environment and to be a driving and vocal force in the local community, to promote fitness and healthy living.
5. We provide activities that are fun, challenging, and designed to help individuals achieve their fitness goals.

Since 2017, the company's mission, vision, and core values have not changed.

New Objectives

At the July 4, 2025, board meeting, the following objectives and priorities were set:

- Determine whether to specialize CFL's traditional fitness gyms for either the under-40, or the over-55, age demographic.
- Improve the company's EBITDA.

Available Cash Flow /Financing

As of the latest board meeting, July 4, 2025, CFL has only $2 million in cash available for strategic investment and no access to further financing; due to the increased number of loan defaults in the last two years among smaller fitness facility operators, lenders have become reluctant to finance fitness companies with fewer than 50 locations. Currently, CFL only has 40 locations (32 fitness gyms and 8 climbing facilities).

The candidate is NOT expected to recap KSFs, SWOT in detail. However, they must draw upon these in their analysis of the strategic options presented.

Key Success Factors (from Capstone 1)

Key success factors (KSFs) in the gym, health, and fitness facility (fitness) industry in Canada include the following:

- Easy access for clients – the facility should be located as close as possible to its members.
- Effective promotion of products and services – the more brand awareness that a facility has, the more members it will attract.
- Offering a wide range of services and multiple locations – this will help attract new members and retain existing members.
- Providing clean facilities with good-quality equipment.
- Providing good customer service.
- Having skilled (trained) employees – employees should be both knowledgeable and friendly/motivational.
- Retaining members – it is usually more costly to bring in new members than to retain existing members.
- Innovation – to be successful, a company in the fitness industry must research and stay up to date with the current trends.

Preferences by Age Demographic

Using the member survey that was recently conducted at CFL's fitness gyms, a clear distinction was found between the preferences of two separate age demographics: under 40 years old, and over 55 years old.

The under-40 age demographic prefers to have access to a wide variety of activities and gym equipment that is modern, high-tech, and able to synchronize with the latest fitness apps and wearable fitness devices. This demographic also prefers to have a wide variety of fitness class instructors who have specialized expertise, and whose fitness classes are higher intensity. Overall, this age demographic values variety and high-tech fitness machines—one consequence of this is that they tend to use the same piece of workout equipment for only a short period of time relative to the older demographic.

The over-55 age demographic does not require access to a wide variety of activities and prefers gym equipment that is simple to use and does not constantly change—they do not enjoy or use high-tech machines. This demographic prefers lower intensity fitness classes (such as yoga and meditation classes), and fitness class instructors who do not change from class to class. Overall, this age demographic values consistency of equipment and classes, and dislikes high-tech equipment that they find harder to use. This demographic tends to use the same piece of workout equipment for a long period of time.

Internal/External Analysis

Strengths, weaknesses, opportunities, and threats (SWOT) analysis

<u>Strengths:</u>

- CFL resolved the dispute with its fitness instructors by increasing their compensation rates. The company now pays their fitness instructors slightly above the average industry amount.
- Since Capstone 1, CFL has successfully diversified the company's revenues through the Zenfit agreement, and by converting eight of the company's fitness gyms into climbing facilities.
- Brian's climbing expertise has helped contribute to the success of the climbing facilities—this expertise could be further leveraged if CFL decides to grow its climbing wall operations by opening more climbing facilities.

Weaknesses:

- CFL's overall number of fitness gym members has continually declined since 2022, largely due to the increase in competition. If CFL's membership rates continue to decline, the company may have to close some of its fitness gyms.
- Given the drop in the number of members at CFL's fitness gyms, the company has attempted to retain its members by reducing its membership prices. This strategy has not worked and has also contributed to the drop in earnings at the company's fitness gyms.
- Rosa resigned her position as CFL's CFO, and wants to sell her shares in CFL as soon as possible. CFL is currently without a CFO and needs to find a replacement.
- CFL only has $2 million available for strategic investment and no access to additional debt financing—this will make it a challenge for the company to expand its operations.
- CFL only has 40 current locations (32 fitness gyms and 8 climbing facilities). Lenders have recently only been willing to provide debt financing to companies that have at least
  50 locations.

Opportunities:

- CFL could specialize in order to cater to one of two very different demographics (under-40 and over-55). Specializing may help to attract new members.
- The popularity of climbing continues to increase and the number of competitors in this market is lower relative to the fitness gym market. CFL can capitalize on this, as well as on the success of its existing climbing facilities, and open more climbing facilities.
- CFL has been offered $12 million for its existing climbing facilities. This cash could be used to reinvest in other areas of the business.
- CFL could become the national distributor for Zenfit products. The current distribution agreement (Western Canada) has so far proven to be successful—CFL may be able to expand this level of success by becoming the national distributor.
- Alternatively, CFL could sell its current Zenfit distribution agreement to an interested party for $9 million. This cash could be used to reinvest in other areas of the business.
- Market research indicates that the under-40 age market is growing significantly faster than the over-55 market—CFL could take advantage of this growth by specializing its gyms to target the younger market.
- However, the over-55 demographic is willing to pay more for a gym membership that suits their preferences. Therefore, by targeting the older segment, CFL would be able to avoid the price war that is currently taking place within the industry.

- CFL could significantly expand its fitness gym operations by purchasing RJ's Health Clubs Limited (RJ). Not only would this acquisition make CFL national, but it could also help CFL access further debt financing, given that the company would own over 50 locations.

Threats:

- In recent years, the fitness industry has seen a large increase in competition for both fitness gyms and fitness machines. CFL's market share has declined because of this. If the current trend of losing members continues, CFL's fitness gyms may not survive.
- Debt financing has become harder to obtain in recent years, as many banks are reluctant to loan money to smaller fitness companies due to the increased number of defaults within this industry segment.

Conclusion

CFL is at a critical moment in terms of how it chooses to focus the company's main revenue driver: the fitness gyms. The company has two alternatives: (1) focus on satisfying the preferences of the under-40 age demographic by offering a wide variety of fitness alternatives and high-tech machines, or (2) focus on satisfying the preferences of the over-55 age demographic by offering more consistency (of classes, instructors, and machines) and low-tech fitness equipment. If CFL does not choose wisely, the company's fitness gyms might not survive.

Although CFL currently has limited access to investment funds, the company has offers to sell its Zenfit distribution agreement and/or its climbing facilities. Therefore, CFL must decide which of the strategic alternatives will help the company best protect its current revenues while also paving the way for future growth.

Summative Assessment #2 (Analyzes the Major Issues)

For Summative Assessment #2, the candidate must be assessed for reasonableness of attempt:

Yes – The candidate sufficiently completed a reasonable assessment of the major issues facing CFL.

Unsure – The candidate attempted to complete a reasonable assessment of the major issues facing CFL.

No – The candidate clearly did not complete a reasonable assessment of the major issues facing CFL.

Technical Competency
2.3.3 Evaluates strategic alternatives

Enabling Competencies
1.1.3 Exhibits ethical behavior by complying with laws and regulations, organizational policies, societal norms and personal ideals
6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems
6.1.3 Demonstrates skepticism, objectivity, due care and persistence when identifying issues
6.2.3 Questions the relevance and tests the quality of information and assumptions in own analyses
6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

This summative assessment is based on Assessment Opportunities #2 to #6.

Assessment Opportunity #2 (Strategic Issue #1 – Fitness gyms: modernize for under-40 market or specialize for over-55 market?)

The candidate is expected to complete both a quantitative and qualitative assessment of which age demographic CFL should target within its fitness gym operations.

Quantitative analysis: The candidate should complete an earnings projection for both options.

Qualitative analysis: The candidate should discuss both the advantages and disadvantages of both target markets, taking into consideration the preferences of each target group.

Conclusion: The candidate should offer a conclusion that incorporates and logically follows from their quantitative and qualitative analyses.

Due to increased competition, CFL's 32 fitness gyms are at risk of going out of business. Market research and CFL's customer survey indicate that there is a clear distinction between the preferences of the under-40, and the over-55, age demographics. For its fitness gyms to survive, CFL wants to focus on satisfying the preferences of one of these groups.

Quantitative Analysis

Based on the information provided by Phillip, a projection for each of the potential target market strategies has been provided below.

Modernize gyms (target market: less than 40 years old)

	Actual	Projection		
	2024	2026	2027	2028
Number of memberships by age				
Younger than 40	10,854	16,281	24,422	36,632
40 to 55	16,653	18,318	20,150	22,165
Older than 55	10,030	2,006	2,006	2,006
	37,537	36,605	46,578	60,803
Revenue (in thousands)				
Gym memberships	$21,396	$20,133	$25,61 8	$33,442
Personal training	13,262	11,935	10,742	9,668
Total revenue	34,658	32,068	36,360	43,110
Operating expenses (in thousands)				
Purchases	1,191	1,191	1,191	1,191
Wages	19,065	20,018	20,018	20,018
Marketing and advertising	1,786	1,786	1,786	1,786
Occupancy costs	5,691	5,691	5,691	5,691
General and administrative	6,691	6,691	6,691	6,691
EBITDA	$234	$(3,309)	$983	$7,733

Specialize gyms (target market: greater than 55 years old)

	Actual	Projection		
	2024	**2026**	**2027**	**2028**
Number of memberships by age				
Younger than 40	10,854	2,171	2,171	2,171
40 to 55	16,653	14,988	13,489	12,140
Older than 55	10,030	12,036	14,443	17,332
	37,537	29,195	30,103	31,643
Revenue (in thousands)				
Gym memberships	$21,396	$18,976	$19,567	$20,568
Personal training	13,262	13,925	14,621	15,352
Total revenue	34,658	32,901	34,188	35,920
Operating expenses (in thousands)				
Purchases	1,191	1,191	1,191	1,191
Wages	19,065	14,299	14,299	14,299
Marketing and advertising	1,786	2,500	2,500	2,500
Occupancy costs	5,691	5,691	5,691	5,691
General and administrative	6,691	6,691	6,691	6,691
EBITDA	$234	$2,529	$3,816	$5,548

Although the number of members is projected to be higher if CFL chooses to focus on the under-40 age demographic, the costs of satisfying this group are much higher relative to the over-55 age group. Therefore, at least for the first two years after the initial conversion, the option that will improve CFL's EBITDA by the highest margin (in accordance with the company's stated objectives) is the over-55 age demographic.

Further to this, the annual cash flow obligation associated with the under-40 age demographic ($7 million) is far greater than that of the over-55 age demographic ($1 million). This is because satisfying the preferences of the under-40 market involves providing the latest and most modern equipment, which comes at a higher cost relative to the equipment that the over-55 market desires. Therefore, from a quantitative perspective, it appears that the over-55 market is the more attractive option.

Finally, it is crucial for CFL to verify the accuracy of the membership forecasts that were provided by Phillip. These forecasts form the basis for the recommendations above, and it is therefore vital to ensure that the fluctuations in membership rates projected are realistic and accurate.

Qualitative Analysis

Modernize gyms (target market: less than 40 years old)

Advantages:

- CFL's market research indicates that this age demographic is growing significantly faster than the market for the over-55 demographic. Therefore, if CFL targets the under-40 age group, the company can take advantage of this growth.
- CFL currently has more members in the under-40 demographic relative to the over-55 demographic; therefore, by catering to the needs of the younger demographic, CFL will be able to satisfy more of its current membership group. This aligns with a KSF of the industry to retain current members, given that it is typically less expensive to retain members than to acquire new ones.
- Modernizing the fitness gyms and catering to the needs of the younger, under-40 demographic would also increase the number of members in the 40-to-55 demographic, given that this demographic has a slight preference for more modern exercise machines.
- Other than Zentracker's lack of ability to connect with wearable fitness devices, the under-40 group likes the machine. Therefore, there is a synergy between this age demographic and CFL's agreement with Zenfit. When Zenfit's new machine becomes available, the under-40 group may become more satisfied with CFL's fitness machines.
- The under-40 group listed climbing as a requested activity in CFL's recent member survey; therefore, there is a current synergy between this target market and CFL's climbing facilities. By focusing on this age group, CFL may effectively cross-sell its existing fitness gym and climbing facility members.

Disadvantages:

- To succeed in this market, CFL will be forced to compete on price—a current trend in the industry is for gym companies to reduce their rates in order to attract more customers. Therefore, the projected $550 annual membership for this demographic may need to be decreased over time.
- The under-40 age demographic prefers to have access to many different types of activities (such as many kinds of fitness classes, martial arts, climbing, swimming, etc.), and strongly prefers variety—it would be a challenge for CFL to provide all these activities, and CFL could therefore lose more members in this age demographic.
- This age demographic's preference for modern and high-tech fitness equipment will drive up CFL's costs—if the company decides to specialize the fitness gyms for this group, it would be forced to continually purchase the newest equipment (this age demographic tends to use the same piece of workout equipment for less time than the over-55 group).

- Community is not important for this age demographic; therefore, CFL would not be able to use this feature of their fitness gyms in order to retain these members.
- Most of the new competitor gyms in the fitness gym market are equipped with modern, high-tech equipment; if CFL chooses to modernize its gyms, it will be forced to compete with many other gym companies.

Specialize gyms (target market: greater than 55 years old)

Advantages:
- The over-55 age demographic is willing to pay more for a gym membership that suits their preferences ($100 more for an annual gym membership relative to the under-40 group). This point is especially important when considering the trend of decreasing membership rates, given the increased level of competition.
- CFL's wage expense would decrease as a result of specializing its fitness gyms for the over-55 market because this demographic prefers to have the same fitness instructor from class to class. This would also simplify CFL's fitness class operations.
- The requested activities of this age demographic are more basic when compared to the younger demographic. It would be much easier for CFL to satisfy the desires of this age demographic, and therefore, it might be easier to retain these members.
- This age demographic prefers to have access to simple, low-tech machines that do not continually change over time. It would therefore cost less for CFL to satisfy the preferences of this age demographic when compared to the under-40 group. This would also help simplify CFL's operations, as machines would not need to be replaced as frequently.
- CFL's operations would be further simplified as a result of this age demographic's preferences for consistent fitness class instructors (the over-55 group prefers to have the same instructor from class to class).
- It may be easier to retain members from this age demographic, given its preference for community. This preference results in a reluctance to change gyms. CFL could cater to this preference by actively developing the community atmosphere of its fitness gyms.

Disadvantages:
- The over-55 group does not use the Zentracker machine by Zenfit because the machine is too complicated. Therefore, there is a conflict between specializing for this group while also having the distribution agreement with Zenfit.
- If CFL decides to focus on this age demographic, the company will lose many of its current members (given that the bulk of CFL's clients are currently in the under-40 and 40-to-55 age demographics). If the transition to the over-55 group is unsuccessful, CFL's fitness gyms are unlikely to be able to stay open. This also violates one of the KSFs of retaining members.

- This would violate CFL's mission of providing state-of-the-art equipment—this is because the preferences of the over-55 market do not align with this aspect of the company's current mission. If the company decides to focus on this area of the market, the mission statement will likely need to be revised.

Conclusion

Given that the over-55 market has both more attractive quantitative and qualitative features, we recommend that CFL choose the over-55 age demographic as the company's target market for its fitness gyms. Although CFL would need to take an initial risk by losing many of its current members aged below 55, the data collected by CFL indicates that this risk would be worth it in the long term. The costs associated with satisfying the older market are significantly lower when compared to the younger demographic and there appears to be much less competition for the older demographic's business.

Assessment Opportunity #3 (Strategic Issue #2 – Become Zenfit national distributor or sell distribution and video production rights?)

The candidate is expected to complete both a quantitative and qualitative assessment of whether CFL should expand its current agreement with Zenfit or sell the current agreement for $9 million.

Quantitative analysis: The candidate should perform a trend analysis of the current agreement's earnings, and provide a revised earnings projection based on that trend analysis. The candidate should compare the expected earnings of the last two years of the existing contract with the$9 million offer that CFL has received for selling the agreement.

Qualitative analysis: The candidate should compare the qualitative advantages and disadvantages of expanding the agreement versus selling it.

Conclusion: The candidate should offer a conclusion that incorporates and logically follows from their quantitative and qualitative analyses.

To date, the Zenfit agreement has worked out well for CFL, and the company now has the opportunity to expand its distribution rights with Zenfit by becoming the exclusive national distributor of Zenfit products. Zenfit has stated that, if CFL does not agree to become the national distributor, Zenfit will not renew the existing agreement when it expires in two years' time.

CFL has also been presented with an offer to sell its existing distribution and video production agreement with Zenfit to an interested party for $9 million. Therefore, CFL must decide what kind of involvement the company wishes to have with Zenfit now and in the future.

Quantitative Analysis

The following revised projection is based on the information that Frank provided in the board meeting. In 2025, the number of units sold has dropped by 20%, and Frank also expects that the number of Zenfit Live subscribers will drop by 10%, relative to the 2024 numbers. According to Frank, these trends are expected to continue. Therefore, to assess the contribution to earnings that CFL can expect from its existing agreement with Zenfit, a revised projection is necessary.

	Actual	Projection	
	2024	**2025**	**2026**
Distributor fees			
Units sold	546	437	350
Total gross sales of Zenfit products	$5,460,000	$4,368,000	$3,494,400
Distributor fee (15%)	819,000	655,200	524,160
Less related direct costs	81,800	81,800	81,800
Annual distributor fee (net)	737,200	573,400	442,360
Video royalty fee			
Number of subscribers	202,500	182,250	164,025
Total annual CFL viewed videos	3,159,000	2,843,100	2,558,790
Flat royalty rate per video viewed	0.75	0.75	0.75
Annual video royalties (net)	2,369,250	2,132,325	1,919,093
EBITDA from Zenfit agreement	$3,106,450	$2,705,725	$2,361,453

Based on the revised projection, CFL can expect to earn approximately $5 million during the final two years of the existing agreement. The original projection that CFL completed (provided in Appendix V) appears to be too optimistic, just as Frank stated in the board meeting. This downward trend in the popularity of Zenfit's products and services can already be seen in the actual 2024 earnings figures relative to 2023. It is possible that the popularity of Zenfit products has already peaked.

However, as Sandra mentioned, Zenfit is set to release a new Zentracker machine that may revitalize the popularity of Zenfit and its products and services, and restore the Zenfit sales figures to match the projections. Conversely, that outcome is questionable, given the trend discussed above, and the fact that there are many other technologically advanced fitness machines that are set to enter the market in the coming months and years. This increase in competition may further drive down the demand for Zenfit products.

Also, in order to retain exclusivity as part of the proposed national distributor contract, CFL must achieve a minimum of $10 million in annual sales. It is questionable, from the above projection and trend analysis, whether this will be possible.

<u>Sales offer</u>

It appears that the offer that CFL has received, to sell its existing distribution and video production agreement with Zenfit for $9 million, is very attractive. This is because the revised projection shows the projected earnings that CFL can expect from the existing contract to be roughly $5 million. Therefore, by selling now, CFL would significantly increase the amount of cash generated through the agreement.

Before a decision is made, CFL should verify whether Frank's assertions are correct. The company should also seek to project what kind of earnings CFL could expect if the company was to expand its existing agreement with Zenfit. However, based on the information that has been provided, it appears that selling its existing distribution and video production rights is the most attractive option from a quantitative perspective.

Qualitative Analysis

<u>Advantages:</u>

- Both aspects of the agreement with Zenfit (the distribution agreement and the production of Zenfit's live streaming videos) have so far been successful. The agreement with Zenfit has resulted in an increase to CFL's EBITDA. Selling the agreement would result in a decrease to CFL's EBITDA, which would violate CFL's objective to increase EBITDA.
- Zenfit has a new, technologically advanced machine that is set to come out next year. This new machine integrates well with most wearable fitness devices—in CFL's member survey, the under-40 group stated that they stopped using Zentrackers because of its inability to connect to wearable fitness devices. The new machines may help to increase the sales of Zenfit products among this age demographic. This aligns with the KSF of staying up to date with current trends.

- The new Zenfit machine has received great reviews by early users—this should help give CFL confidence that the new machine will be well received once it is released.
- CFL currently does not have much cash to invest. Expanding the Zenfit agreement to become the national distributor does not require an upfront cash investment and would therefore not hurt CFL's already strained cash flow.
- If CFL does not agree to become the national Zenfit product distributor now, Zenfit will not renew CFL's contract when it comes due in 2026. Losing the agreement would result in a drop in the company's EBITDA, which would violate one of CFL's objectives.
- If CFL decides to specialize the fitness gyms for the under-40 age demographic, there could be a synergy between Zenfit's new product and the preferences of this demographic (who prefer modern, high-tech fitness machines that sync with wearable fitness devices). This synergy will be enhanced, given that the national distributor has the right to purchase Zenfit products for its own use at a discounted price of 15% off the normal retail price (whereas the current agreement provides CFL with a 10% discount on Zenfit products).

Disadvantages:

- Both aspects of the agreement are trending downwards—in 2024, the annual sales of Zenfit products, and the annual video royalties, decreased relative to 2023. It may be that the popularity of Zenfit products has started to decline.
- There is an increasing number of fitness streaming services that are available. This new competition will make it more difficult for CFL to retain current users and expand to attract new users.
- There are many other new, high-tech fitness machines that are expected to be released in the next few months and years; this will increase the competition that Zenfit products face, and may result in a drop in popularity/sales of Zenfit products.
- If CFL decides to specialize the fitness gyms for the over-55 age demographic, the Zenfit product line is probably not the best fit for a strategic partnership. The over-55 group prefers low-tech equipment, and explicitly stated that they only rarely use the Zentracker machine because it is too complicated.

Option to sell current Zenfit distribution/video production rights to third party

Advantages:

- By selling its existing agreement, CFL would simplify its operations, as the company would no longer be responsible for producing exercise videos and selling Zenfit equipment. This simplification of operations would allow CFL to focus more attention on its fitness gyms—the company's core business.
- CFL would no longer be forced to participate in this highly competitive market; therefore, the company would be able to reduce the amount of uncertainty that is inherent in a highly competitive marketplace.

- Selling the agreement would provide CFL with a significant influx of cash that could be used to help stabilize the company's financial position, and would allow the company to invest in other areas that support the company's stated mission and vision.

Disadvantages:
- CFL would lose the exposure that the company has attracted through producing and publishing workout videos using the Zentracker machine—this could result in a loss of brand exposure.
- By selling, CFL would lose this revenue stream, which is largely based on the at-home fitness market. Selling would cause CFL to lose this diversification of revenue, and the company would therefore become more reliant on its fitness gyms, which have been suffering lately. This goes against the KSF of offering a wide range of services.
- If CFL sells its current distributor and video production rights, the company will lose its current 10% discount on all Zenfit equipment purchases. If CFL continues to purchase Zenfit equipment after the sale, the equipment cost will increase.

Conclusion

Based on the information that has been provided, as well as when considering CFL's current state and objectives, it is recommended that the company sell its existing Zenfit agreement for $9 million. Based on the declines that have been experienced and are projected, the popularity of Zenfit products may have already peaked. Also, given all the new competition that is set to enter the marketplace, there is a risk that Zenfit is unable to regain its popularity with its new Zentracker machine, despite the great reviews it has received. Selling the agreement would provide CFL with a large influx of needed cash. This cash can be put to good use in helping CFL secure its fitness gyms, as well as expand into other areas, such as the climbing facilities or through the acquisition of RJ.

Assessment Opportunity #4 (Strategic Issue #3 – Sell or expand climbing facilities?)

The candidate is expected to complete both a quantitative and qualitative assessment of whether CFL should open additional climbing facilities or if the company should instead sell all its climbing facilities for $12 million.

Quantitative analysis: The candidate should calculate the approximate value of the existing climbing facilities. The candidate should then compare this figure with the $12 million offer that CFL has received for selling its current climbing facilities.

Qualitative analysis: The candidate should compare the qualitative advantages and disadvantages of expanding the company's climbing facilities versus selling them.

Conclusion: The candidate should offer a conclusion that incorporates and logically follows from their quantitative and qualitative analyses.

Since CFL's first eight climbing facilities opened in 2023, the project has surpassed the company's original expectations. The company can now choose to expand this area of its business by opening additional climbing facilities. CFL must decide whether this course of action is suitable, given the company's stated objectives and the trends in the marketplace.

Further, the company has received an offer to sell all of its current climbing facilities for $12 million, which would provide CFL with a large influx of needed cash.

Quantitative Analysis

Sales offer analysis

	Actual	
	2023	**2024**
Number of members	3,500	3,920
Annual membership rate	$660	$660
Revenue		
Annual memberships	$2,310,000	$2,587,200
Day passes	2,079,000	2,328,480
Special events	1,201,200	1,345,344
Other	1,339,800	1,500,576
Total revenue	6,930,000	7,761,600
Expenses		
Wages	1,455,300	1,629,936
Purchases	485,100	543,312
Marketing	207,900	232,848
Occupancy costs	1,400,000	1,400,000
Other	1,039,500	1,164,240
Amortization	622,222	622,222
Total expenses	5,210,022	5,592,558
Operating income	$1,719,978	$2,169,042
Add back: amortization		622,222
EBITDA		2,791,264
EBITDA multiplier		6
Value of climbing facilities business		$16,747,584

The current value of the climbing facilities business is greater than the offer value of $12 million. Therefore, from a purely quantitative standpoint, CFL should not accept the purchase offer as is. Moreover, the membership numbers of the existing climbing facilities are projected to increase as the popularity of climbing continues to increase. The approximate value of the climbing facilities, as calculated above, may therefore be understated.

Expansion plans analysis

CFL can expand its climbing facility operations into six new locations that have been identified by Brian as being suitable. Brian mentioned that he expects the new climbing facilities will outperform CFL's existing climbing facilities. Based on that assumption, the following analysis calculates the length of time it would take CFL to recoup the original investment cost that is required to open a new climbing facility.

EBITDA (2024)	$2,791,264
Number of climbing facilities	8
EBITDA per location	$348,908
Cost to open each new location	$850,000
Payback period (years)	2.44

It would therefore only take CFL approximately 2.5 years to repay the cost of the investment for each new location opened (assuming similar revenue levels are attainable). Because climbing facilities are becoming more popular, it is possible that the performance of these facilities is better than the forecast above. If this current industry trend continues, the climbing facility investment would take even less time to pay back. However, it is also important to note that, as soon as CFL has over 10 climbing facilities, the company will need to hire an additional senior manager to assist Brian. This increase in cost will increase the payback period.

Qualitative Analysis

Advantages:

- The conversion of eight fitness gyms into climbing facilities has proven to be successful. The performance of the current climbing facilities has surpassed expectations. CFL could build on this success by acquiring new locations to convert into climbing wall facilities.
- The popularity of climbing has recently grown, and this trend is expected to continue—CFL could take advantage of this growth in popularity by opening new climbing facilities.

- Brian's experience with climbing has contributed to the success of CFL's facilities. CFL could leverage Brian's ability to create enjoyable facilities by opening more.
- The members of CFL's current climbing facilities are very satisfied; this indicates that this aspect of CFL's business is stable and has the chance to grow. Retaining members is a KSF for CFL, and the climbing facilities appear to be quite successful at this.
- Climbing is one of the activities that the under-40 age demographic said they enjoy—this is another indication of the increasing popularity of this activity.
- The climbing facilities business does not seem to have a lot of competition. CFL could capitalize on this by expanding the climbing wall operations to gain market share before any new competitors decide to enter the market.
- The proposed expansion of the climbing facilities involves locations that are not currently CFL fitness gyms; therefore, the company will be able to avoid the conflicts that arose when the initial climbing facilities were converted from existing fitness gyms.
- If CFL allows its members access to both kinds of facilities with only one membership, it might attract more members to all its existing locations (both the fitness gyms and the climbing facilities). This synergy would be especially valuable if the company decides to focus its fitness gyms on the under-40 age demographic (who have expressed an interest in climbing).

<u>Disadvantages:</u>

- The initial conversion of the first climbing facilities created some brand confusion among CFL's members—the proposed expansion could worsen this brand confusion. However, CFL would likely be able to mitigate this risk through a clear messaging campaign that differentiated the two products.
- Although CFL has avoided any major liability issues relative to injuries sustained at the company's climbing facilities, there is a clear risk that the company could face additional liability concerns in the future. By opening new climbing facilities, the probability of future liability issues will increase.
- As soon as the company has over 10 climbing facilities, CFL will need to hire an additional senior manager to help Brian with management of the climbing facilities. This may result in a reduction in the quality of service provided, given that Brian's expertise and involvement in the current climbing facilities has been an integral part of the project's success.

- Based on the information provided in Appendix III (preferences by age demographic), it does not appear that the potential over-55 target market has an interest in climbing. Therefore, if CFL decides to target this demographic for its fitness gym facilities, CFL may have a harder time cross-selling its members on the climbing facilities. However, given that the fitness gyms and the climbing facilities are two different products with separate memberships, if CFL decides to specialize the fitness gyms for the over-55 age demographic, the performance of the climbing facilities is unlikely to be adversely affected.
- If CFL decides to specialize its gyms for the over-55 age demographic, given that an over-55 specialized fitness gym and a climbing facility are two distinct types of business, there could be some brand confusion.

Conclusion

Based on the information provided, CFL should not accept the current offer that the company has received to sell the climbing facilities for $12 million. The current climbing facilities appear to be worth more than this, and the popularity of climbing continues to grow. Therefore, based on the success of the current climbing facilities and the further suitable locations that Brian has identified for expansion, CFL should strongly consider growing the number of climbing facilities that the company has. This will help satisfy the board’s objective to increase CFL’s EBITDA. However, as the amount of cash that CFL has for capital investment is limited, before a decision to expand is made, CFL will need to assess whether it has the resources available for this when considering the other strategic alternatives that the company chooses to pursue.

Assessment Opportunity #5 (Strategic Issue #4 – Acquire RJ’s Health Clubs?)

The candidate is expected to complete both a quantitative and qualitative assessment of the potential acquisition of RJ’s Health Clubs.

Quantitative analysis: The candidate should complete a financial analysis of the potential acquisition of RJ’s Health Clubs. This analysis could include a projection of either age demographic that CFL is considering targeting within AO#2.

Qualitative analysis: The candidate should discuss the qualitative advantages and disadvantages of the potential acquisition of RJ’s Health Clubs.

Conclusion: The candidate should offer a conclusion that incorporates and logically follows from their quantitative and qualitative analyses.

RJ's Health Clubs Limited (RJ), a company with similar operations to CFL's current fitness gyms, is being sold for $7.5 million. The asking price is significantly lower than what RJ was purchased for only three years ago. If CFL can determine how to improve RJ's performance, CFL could significantly expand its operations and footprint, given that RJ's 25 gyms are located throughout Eastern Canada.

Quantitative Analysis

Based on the information provided by Phillip in Appendix VII, it is clear that RJ's business is unsustainable in its current form. Over the past three years, the company's performance has decreased significantly and, if the current downward trend continues, RJ's earnings will enter a loss position. This may be due to the strategies that RJ has utilized in its attempt to turn the company around (such as by increasing its marketing, and the number and variety of fitness classes that RJ offers its members).

As stated by Phillip, due to a lack of investment capital, RJ has been unable to keep up with its local competitors in terms of providing its members with the latest and best high-tech exercise equipment. This has resulted in a continual drop in membership. However, on examining the number of memberships within each major age demographic, the number of members within the over-55 age category has been increasing. This may be due to this age demographic's preference for less high-tech machines.

The following analysis will assess the potential result of focusing RJ's operations on this age demographic. Given that CFL's fitness gyms and RJ's gyms share a similar format, the data provided in Appendix IV was used to create this projection.

	Actual 2024	Projection 2026	2027	2028
Number of memberships by age				
Younger than 40	3,528	706	706	706
40 to 55	7,836	7,052	6,347	5,712
Older than 55	8,174	9,809	11,771	14,125
	19,538	17,567	18,824	20,543
Revenue (in thousands)				
Gym memberships	$10,745,900	$11,418,550	$12,235,600	$13,352,950
Personal training	6,344,000	6,661,200	6,994,260	7,343,973
Total revenue	$17,089,900	$18,079,750	$19,229,860	$20,696,923
Operating expenses (in thousands)				
Purchases	941,895	941,895	941,895	941,895
Wages	7,054,050	5,290,538	5,290,538	5,290,538
Marketing and advertising	1,207,050	1,207,050	1,207,050	1,207,050
Occupancy costs	3,453,500	3,453,500	3,453,500	3,453,500
General and administrative	4,277,021	4,277,021	4,277,021	4,277,021
EBITDA	$156,384	$2,909,746	$4,059,856	$5,526,919

If CFL targets the over-55 age demographic within RJ's existing locations, the company appears to have a significant opportunity to improve the performance of RJ's gyms. Not only would RJ's revenue increase but the company's expenses would also decrease significantly.

Based on the annual EBITDA multiplier of six that has been used to value exercise and recreation facilities in the recent past, the value of RJ (based on the projection above) would appear to be: $17.5 million at the end of 2026, $24.4 million at the end of 2027, and $33.2 million at the end of 2028.

Before a decision is made, it is very important for CFL to verify whether the membership trends provided by Phillip in Appendix IV would apply equally to RJ's current operations. However, based on the analysis provided above, CFL would benefit greatly by purchasing RJ and converting its gyms to target the over-55 age demographic.

Qualitative Analysis

Advantages:

- With the acquisition of RJ, CFL could make a large stride toward achieving its mission and vision, given that the company's operations would expand significantly; however, this outcome is contingent on CFL's ability to make RJ profitable once again.
- RJ's existing locations share a similar format to CFL's fitness gyms; therefore, the acquisition of RJ would be uncomplicated from an operational perspective, given that CFL has plenty of experience in this area.
- Each of RJ's gyms is equipped with a yoga and meditation studio. Based on CFL's recent member survey, yoga and meditation are sought-after activities within the over-55 age demographic. This aligns well with CFL's KSF of offering a wide range of services.
- The acquisition of RJ's 25 gyms would significantly increase the size of CFL's operations. One benefit of this is the potential to access additional financing after the acquisition is made, given that many banks have become reluctant to lend to gym companies with fewer than 50 locations. With CFL's 40 existing locations plus RJ's 25 locations, the company would surpass that figure.
- If CFL purchased and then refocused RJ's gyms to appeal to the over-55 market, the company would not be forced to compete on price, given that there are fewer competitors in this market and because this demographic is willing to pay more for a membership.
- As part of the acquisition, CFL would not be required to retain RJ's existing board members. CFL's current business model and direction will therefore not be influenced by any incoming board members, which will help to facilitate a smooth transition upon acquisition. CFL may also be able to find a suitable replacement for Rosa from an existing RJ board member, which could help ease the transition after the purchase is complete.
- All RJ gym facilities are located in Eastern Canada; therefore, if acquired, CFL would increase its brand exposure, and become a national brand.
- The members of RJ are currently satisfied with the variety of fitness classes offered—this may help CFL reduce the number of members who leave RJ for a different gym that better satisfies them in this area.

Disadvantages:

- To date, RJ has been unable to compete with the gyms that offer modern facilities, given the company's lack of available cash needed to purchase the latest high-tech equipment. Therefore, if CFL decides to target the under-40 age group, the acquisition of RJ does not appear to make strategic sense.

- RJ’s membership numbers among the under-40 and the 40-to-55 age demographics have been in decline—as stated by Sandra in the board meeting, the under-40 age demographic is growing significantly faster than the older demographic. If CFL acquires RJ and then targets the over-55 market, CFL would not be able to take advantage of this growth.
- Despite its ongoing effort, RJ has been unable to improve the performance of the company over the past three years—it is not clear whether it would be possible for CFL to succeed either.
- As part of the acquisition, all of RJ’s current lease agreements, assets, and staff members would be transferred to CFL. CFL needs to conduct an adequate amount of due diligence over these aspects of RJ’s business to ensure that they meet the standards of CFL’s current business model.
- RJ’s current equipment is outdated and would therefore require replacement, especially in order to satisfy the preferences of the under-40 and the 40-to-55 age demographics.
- CFL has never had operations in Eastern Canada; therefore, the company lacks knowledge of that market. This could result in unforeseen challenges if CFL tries to apply its business model to fitness gyms in Eastern Canada.
- Expanding operations to Eastern Canada would also increase the logistical challenges in operating and managing the company. Therefore, this acquisition could hamper CFL’s ability to manage the business in the same way that it currently does.

Conclusion

Similar to the analysis performed regarding CFL’s choice of which age demographic to target at the company’s fitness gyms (AO#2), if CFL purchases RJ and refocuses on the over-55 age demographic, the company could be able to increase revenue, reduce costs, and limit the annual investment required for the purchase of gym equipment (given the preferences of the over-55 group). This appears to be the only avenue toward profitability left for RJ to take, as the company has already exhausted its options relative to attracting more members.

However, based on the analysis above, the acquisition appears to be a good strategic investment for CFL, should the company refocus RJ’s gyms to appeal to the preferences of the older demographic. CFL should do further research to verify that the assumptions made within the analysis above are reasonable; if so, this acquisition is recommended.

Assessment Opportunity #6 (Strategic Issue #5 – Governance: find a suitable replacement for Rosa)

A competent candidate will discuss whether either Louisa Rice or Albert Fong is a suitable replacement for Rosa. The candidate should consider how these two options for a board member/shareholder replacement align with their recommendations on the other strategic options that are available—especially AO#2 (which age demographic CFL should target at its fitness gyms).

The candidate should offer a recommendation that incorporates and logically follows from their analyses within the other strategic options that are available to the company.

Rosa decided to resign as a board member and as CFL's CFO. She also wants to sell her shares of CFL (1,000 Class B common shares) as soon as possible. Therefore, CFL needs to find a suitable replacement for Rosa on the company's board.

Louisa Rice

<u>Advantages:</u>

- Louisa is a CrossFit champion who has a large following on social media—this aligns well with CFL's practice of including famous athletes in the company. Her following on social media would likely bring more attention to CFL; therefore, she might help build the company's brand awareness.
- Louisa has the capital required to buy Rosa's shares.
- Louisa's knowledge of fitness and CrossFit would help CFL develop challenging fitness classes that could be rolled out at all of CFL's fitness gyms—this approach to fitness would appeal to the under-40 market (given that this target market prefers intense fitness classes).

<u>Disadvantages:</u>

- As Louisa does not appear to have any experience in corporate finance, CFL would not be able to use Louisa as a suitable replacement for the company's CFO position. Therefore, if CFL decides to elect Louisa to the board, the company would still need to find a CFO.
- Louisa's fitness orientation (CrossFit, highly intense fitness class structure) does not align with the preferences of the over-55 age demographic. If CFL decides to pursue that target market, Louisa might not be the best choice.

Albert Fong

Advantages:

- Albert has a professional history in corporate finance and would therefore be able to replace Rosa as one of CFL's board members, as well as the company's CFO.
- Albert focuses on less intense exercise and has a certification to train others in Pilates and yoga. There is therefore a synergy between Albert and the over-55 age demographic (who value lower-intensity fitness classes).
- Albert lives in Quebec; therefore, if the company decides to acquire RJ, Albert would likely be able to add value to this new aspect of CFL's operations, given that he lives in Eastern Canada.

Disadvantages:

- Albert no longer competes professionally in his chosen sport, boxing. Therefore, the company would not be able to leverage his athletic celebrity status as they would with Louisa.
- It is unclear whether Albert has the capacity to buy Rosa's shares of CFL—the company will need to verify this.

Other Options

As this is an important position, CFL should take its time in making the decision. The right person should be found for the job. If it is determined that neither Louisa nor Albert is a good fit, CFL should continue its search for a suitable replacement. For example, if CFL acquires RJ, a replacement for Rosa could be found from RJ's existing board members.

Conclusion

Louisa appears to be the best option for CFL if the company decides to focus its fitness gym operations on the under-40 age market, because Louisa's expertise appears to align best with the preferences of that age demographic. However, if CFL decides to elect Louisa, the company will still need to find a suitable replacement for CFL's CFO.

Albert appears to be the best option for CFL if the company decide to focus its fitness gym operations on the over-55 age market, because Albert's expertise appears to align best with the preferences of that age demographic.

Therefore, CFL should replace Rosa with the person who best aligns with how the company decides to focus its fitness gyms: Louisa for the under-40 crowd, and Albert for the over-55 group.

Summative Assessment #3 (Conclude and Advise)

For Summative Assessment #3, the candidate must be assessed for reasonableness of attempt:

Yes – The candidate provided reasonable conclusions for each major issue.

Unsure – The candidate attempted to provide reasonable conclusions for each major issue.

No – The candidate clearly did not provide reasonable conclusions for each major issue.

Enabling Competencies
6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions
6.3.2 Articulates limitations to recommendations
6.3.3 Applies decision criteria to choose among viable alternatives
6.3.4 Ensures that decision criteria do not conflict with professional ethics and values

The candidate is expected to provide an overall conclusion that integrates the analyses of all five major issues: which age demographic to target at the company's fitness gyms; whether to expand or sell the Zenfit agreement; whether to expand or sell the company's climbing facilities; whether to acquire RJ; and which person to elect to CFL's board as a replacement for Rosa.

The recommendations should be consistent with the analyses performed. As well, an overall conclusion should be presented that acknowledges the company's available investment capital and integrates the analysis of each major issue in a logical manner.

The candidate should consider whether the available investment options will help CFL improve the company's EBITDA (a stated objective of the engagement). As every available investment aligns with the company's mission and vision statements, these aspects of the situational analysis did not play a major role in the assessment of which options CFL should proceed with.

The candidate was also asked specifically which age demographic CFL should target as members for its fitness gym operations, and should therefore make a clear recommendation.

Recommendations on Specific Issues

Target market for fitness gyms

Given the analysis performed, it appears that targeting the over-55 age demographic gives CFL the best chance of improving the performance of its fitness gym operations. This is because there is less competition for this market and, based on the information provided, it would appear that targeting this group would have the best effect on the company's EBITDA.

Zenfit agreement: expand to become national distributor or sell for $9 million

The popularity of Zenfit products and services appear to be in decline. This trend may become even worse when all the new projected products and services enter the market, and make it even harder for Zenfit to compete. Given the uncertainty around Zenfit's future popularity and performance, and the fact that CFL needs additional cash flow, it is recommended that CFL sell this contract to the interested party. The $9 million influx will allow CFL to make investments in the other options that are presently available.

Climbing facilities: expand or sell for $12 million

The demand for climbing is increasing and, so far, the company's climbing facilities have been very successful, and continue to contribute to the company's earnings. Brian's expertise has been an asset, and CFL can leverage his expertise further through an expansion. Therefore, this option aligns well with the company's objective to improve CFL's EBITDA. In addition, given that the value of the climbing facilities is greater than the option to sell the eight facilities, it is not recommended that CFL sell. If CFL has the cash available, the climbing facilities would be an excellent option to invest in.

Acquisition of RJ's Health Clubs

Although risky, based on the information provided, CFL should acquire RJ. However, before this decision is made, more due diligence is required, to ensure both that the financial information provided by RJ is accurate, and that the membership projections made by Philip will realistically apply to RJ. If these projections are determined to be accurate, the company should purchase RJ and convert the facilities to adhere to the preferences of the over-55 age demographic.

Overall Conclusion

CFL should target the over-55 age demographic by converting the company's fitness gyms to suit that market's preferences (therefore, it might also be necessary to amend the company's mission and vision statement to acknowledge this focus). Next, CFL should sell the Zenfit agreement for $9 million and acquire RJ. This will make CFL a national brand and will also increase the likelihood that CFL can obtain further debt financing. With whatever cash CFL has left over, the company should expand its climbing facilities. Finally, as the company gains additional investment capital in the future, it can continue to expand its climbing facilities by opening the remaining locations.

A summary of the cash required to follow this recommendation is as follows:

Cash currently available (SO#1)	$ 2,000,000
Cost to specialize gyms for over-55 age group	(1,000,000)
Cash available if Zenfit is sold	9,000,000
Cost to purchase RJ	(7,500,000)
Cash remaining	$ 2,500,000
How many new climbing gyms to open ($850,000 each)	3

Other recommendations are acceptable if they are supported and take into consideration the financing required.

Summative Assessment #4 (Communication Hurdle)

For Summative Assessment #4, the candidate must be assessed for reasonableness of attempt:

Yes – The candidate adequately communicated their response.

No – The candidate clearly did not adequately communicate their response.

Insufficient communication in a candidate's response would generally include some of the following:

- The reader needs to re-read sections several times in order to gain an understanding.
- It is not clear what point the candidate is trying to make.

- The quantitative analysis does not make sense because of a lack of labelling or illogical ordering.
- There is an excessive amount of spelling and grammatical errors.
- Unprofessional language is used.

Summative Assessment #5 (Overall Assessment)

For Summative Assessment #5, the candidate must be assessed in one of the following, based on their overall performance:

Clear Pass – Overall, the candidate provided an adequate response, clearly meeting the minimum standards for each of the summative assessments above.

Marginal Pass – Overall, the candidate provided an adequate response, with some errors or areas of omission, but the underlying key concepts were there.

Marginal Fail – Overall, the candidate provided an attempt at a response, one that contained several errors or where the analysis was incomplete.

Clear Fail – Overall, the candidate did not provide an adequate response; the response was deficient in multiple areas.

To be assessed a Pass, the candidate is expected to perform adequately in all the summative assessments and demonstrate that, overall, they addressed the issues of all of the shareholders.

In making their overall assessment, markers were asked to consider the following:

1. Did the candidate step back and see the bigger picture, and then address the broader issues identified?
2. Did the candidate prioritize the issues by discussing the major and minor issues in appropriate depth?
3. Did the candidate use both quantitative and qualitative information to support their discussions and conclusions?
4. Did the candidate use the appropriate tools to perform quantitative analysis?
5. Did the candidate use sufficient case facts (current case and Capstone 1 case) about the external and internal environment to support their discussions?
6. Did the candidate communicate their ideas clearly, integrating and synthesizing the information?

SAMPLE RESPONSE – CFL VERSION 1

Below is an actual passing candidate response.

Situational analysis

From Capstone 1

Vision

We strive to motivate and help adults meet there goals.

Mission

We are company dedicated to educating adults on fitness with state of the are equipment, and ever changing group classes. We also strive to promote a healthy and fit lifestyle in our communities.

Corporate values:

1. Our employees will work together to meet the goals and mission of CFL. Every member, staff, and employee is treated with respect and dignity.
2. We strive to have state of are equipment, and offering ever changing group classes with new technology , trends and fads.
3. We want to build friends in our environment, and promote a healthy and fit lifestyle among our local communities.

Key Success Factors (KSF)

- Brand recognition through promotion
- Geographical access to our clients
- Clean and up to date equipment
- Offer multiple services to clients.
- High skilled and knowledgeable employees.
- Retention of members.
- Innovation through trends and technology.

Current Situational analysis:

Targets:

- Improve EBITDA

SWOT:

Strengths:

- Resolved issue with employee morale with competitive wages, this means the employees will be happier and produce a better service for the members, a key for member retention.
- CFL is cash positive, they have $2 million to spend on strategic objectives, this is a huge improvement from a few years ago when they were tight for cash.
- CFL removed the trainers that were selling the supplements, this means they are only employing staff that have Morales, which will help member retention as they will be able to trust the staff more.
- The Zenfit and Climbing studios have done better than originally budgeted, this is great as it will increase revenues for CFL which will increase the overall EBITDA going forward. It also allows the potentially be more risky with a strategic option, as the 2 options remain growing for the next few years.

Weaknesses:

- Number of members continues to decline for CFL, this will lead to lost revenue and lower EDITDA. They have dropped by 15000 in 3 years. This could cause a going concern issue for CFL.
- Rosa is stepping away, which means CFL will be looking for a new CFO, this can be difficult to find the right person for the position, which means CFL may be spending more time looking for the right person, rather than focusing on increasing EBITDA.
- Creditors are only extending funding to companies with more than 50 locations, CFL only has 32, which means they will be unable to secure any funding for strategeic plans moving forward.This could limit the options.
- CFL lowered the cost of the annual memberships, this means they will have less revenue which will lead to less EBITDA.

Opportunities:

- The new demand in the market is for devices that members can connect there fitness devices to. This a new market that CFL can jump on.

Threats

- Increase competition from other companies, and they are expanding rapidly.
- The trends are dictating that annual memberships are decreasing in value in the traditional gyms, this means CFL may need to cut even more of there prices going forward to remain competitive in the market, which will lower revenue and overall EBITDA.

<u>Quantitative Analysis:</u>

- CFL has $2 million in cash saved for a strategic option, this means they do have ample cash for if the something does goes wrong, which is an advantage. Cash-flow in any industry is paramount to stay innovative.

<u>Option 1, decide on a demographic for CFL to focus on.</u>

CFL is looking focus on one demographic moving forward, as the "one size fits all" model is not currently working for CFL. The options are to focus on either an under 40 market, or over 55 market. This will be done by either modernising the current gyms (<40), or specialising them (55>)

Quantitative Analysis:

From the attached spreadsheet we can see that:

- modernising gyms produces a EBITDA of $8.8 million over the next 3 years.
- Specialising gyms produces an EBITDA of $11.9 million over the next 3 years.

Other financial considerations:

- The annual equipment investments were not taken into account for these calculations, CFL is only focused on EBITDA for these strategies, however it should be noted that modernising the gyms will require a substantial cash injection.
- The projections for the modernising equipment do seem relatively high, although the market indicates the increase, something to consider is the younger demographic generally focus on what is new and trendy in the market. This may lead a lower increase if there is a new fad that CFL does not decide to go with in the future.

Qualitative Analysis:

Pros for Modernising the gyms:

- Modernising the gym with new and up to date equipment ties in with CFL's mission of offering state of the art equipment. This ties directly to the mission and supports it.
- A KSF for CFL is to have updated equipment, the option aligns with the KSF as it will update the equipment each year with a generous budget.

Cons for modernising the gyms:

- In the quantitative analysis, it was stated that CFL has $ 2 million for strategic options, this requires $7 million each, will an expected loss in revenue for the first year. This means CFL may be forced to pursue one of other options which means selling off a rather successful division of CFL.

- One of the KSF is member retention, this model will eliminate 80% of <55 division members which goes directly against CFLs KSF of retaining members.

Pro's for Specialising gyms:

- This aligns with CFL's corporate value of promoting health and fitness in the community. It was stated that members are reluctant to change gyms because of the connection to the community. This supports that corporate value.
- The cost to maintain the gyms is only $1 million compared to the $7 million of the other option. This will lead to more cash flow available for CFL to pursue other strategic options.

Con's for Specialising gyms

- CFL will only commit $1 million to the fitness equipment. This goes against the second corporate value, of promotion state of the are equipment to members. This does not support that corporate value.
- It was also stated that this demographic's least important aspect of the fitness facility is high end equipment. this goes against CFL's mission of providing state of the art equipment to members. This goes against CFL's mission.

Recommendation

I recommend that CFL focuses on specialising the gyms for the over 55 market. This is due to that they produce a higher EBITDA over the next 3 years, as well as it only requires an annual investment of $1 million, which CFL can pursue given it's limited cash limit. This option also aligns with CFL's corporate value of promoting health and fitness in local community, which is what the >55 demographic stated as its most important factor to the facility.

<u>Option 2 Become Zenfits exclusive national distributor.</u>

Quantitative Analysis:

From the attached spreadsheet we can see that this option will produce a EBITDA of $2.9 million in 2025 and $2.7 million in 2026. CFL also has the option to sell this contract for $9 million.

Other financial considerations:

- It was mentioned in the case that numbers are likely to decrease, however it was also stated that there is a new surge in demand for technology that integrates with personal fitness devices. the new technology that Zenfit is supplying can integrate with personal fitness devices. This means that the demand for Zenfit may be higher than originally projected, which would increase the revenues going forward, and provide a higher EBITDA.

Qualitative Analysis:

Pro's:

- The new zentracker is technologically advanced, which aligns with CFLs KSF of innovation through new technology. This aligns with the KSF and will allow CFL to be more innovate going forward.
- The Zentracker can integrate with almost all wearable fitness devices. This will help CFL capitalise on the opportunity for the new demand of integrating personal trackers will equipment. This will allow CFL to capture a new market which will lead to increased EBITDA through revenue.This option does not require any cash investment, which means CFL can pursue it without having to spend any of the $2 million cash-flow. It will also allow CFL to spend that money on another strategic option rather than being tied into 1 option.
- CFL has the option to sell the proposal right now for $9 million. This will help CFL overcomes it weakness of not having available funding for new strategies. It was stated that CFL would not be able to secure funding, so this sale will give CFL a total of $11 million to spend on other options going forward.

Con's:

- If this is not pursued, then Zenfit will not renew the contract with CFL in 2 years. the Zenfit proposal has done better than projected, which means, if CFL loses it, it will lose a significant amount of profit which will lower the EBITDA going forward.
- Going forward, the projections from Frank show a 20% drop in unit sales, and a 10% drop in annual subscribers. This will lower the overall revenue for the year, which will lead to a lower EBITDA. It also may result in a trend of continual decrease over the next few years which will further impacts CFL's EBTIDA for worse.
- It was stated that for the contract to occur, CFL must be able to have 10 locations in eastern Canada to show these to potential customers, CFL is currently only in western Canada, this will require CFL to expand out east, which only option at this point is RJ's. This will not give CFL the option if it will pursue RJ's, If CFL decides to do this, it will need to purchase RJ's.

Recommendation

I recommend that CFL sell of this contract for $9 million. This is due to the fact that CFL will likely lose the contract in 2 years anyway as the option for CFL to expand into Eastern Canada is through the RJ's proposal with was not recommend (discussed below). The projected sales for the units are also going to decrease as will the subscribers which will lower CFL's overall EBITDA. CFL will also begin catering to >55 members (discussed above) who have stated that they use the machines "very rarely, as the machines are too complicated".

<u>Option 3 - Open 6 new rock climbing facilities.</u>

Analysis:

Quantitative:

From the attached spreadsheet, I have calculated an EBITDA of $2.2 million for 2025.

Some considerations:

- It was mentioned that CFL would need to hire a senior manager to help Brian with managing all the facilities. This has not been taken into account as there was no estimate for how much they would cost. Once that number has been determined, it should be factored in, it will increase wages which will decrease overall EBITDA.
- Another thing to consider is that CFL will be opening these locations, I will assume that not all 6 faculties will be available to public for the start of 2026 as it is already July. Will that being stated, it will be unlikely that all 6 will be open for the year, and the projections are such that they project over the annual year. This needs to be considered, and a updated projection should be prepared once the timeline is known.

Qualitative Analysis:

Pro's:

- A KSF for CFL is member retention, as the rock climbing studios have been welcomed by all age demographics, CFL will be able to retain all age demographics which meets the KSF.
- CFL has received an offer on $12 million to purchase the 8 existing facilities. This would give CFL the flexibility to pursue multiple strategic options, as they would $14 million in cash to spend. It would also help overcome a weakness as CFL cannot apply for funding, which could limit the amount of strategies they pursued.
- It was stated that there was not much competition in the rock climbing market, this means CFL can continue to lead to market, and not have to worry about members leaving, or cutting membership prices like in the general fitness gym market.

- By opening 6 new facilities, this aligns with CFL's KSF of geographical access to clients, it will provide 6 new gyms at different geographical regions in which members can access. This meets the KSF.

Con's:

- A KSF is brand recognition for CFL, it was stated that with the opening the rock climbing facilities, there was some confusion among the members. This goes against the KSF as now CFL has a brand in which some member cannot understand it.
- Although this option caters to all demographics, it did state that some members were angry that the fitness gyms closed in order to open these rock-climbing facilities. This goes against CFL's KSF of member retention, as members were lost due to transition.
- Opening 6 gyms will cost $5.1 million to pursue, this exceeds the amount of cash that CFL has available which was stated at $2 million. CFL also has the weakness of being unable to secure funding due to the lack of gyms.

Recommendation

I recommend that CFL pursue this option, and begin constructing/buying/developing the gyms immediately. This can be done, as CFL has sold off the Zenfit contract (discussed above) and has ample cash to begin development. This is due to option aligning with member retention, as all demographics have stated that they enjoy the rock-climbing facilities. It was also produces a substantial EBITDA of $2.2 million per year, and CFL has the majority of the market share, will it being stated there are no real competitors in the rock-climbing market.

<u>Option 4 - Purchase RJ's Health clubs limited.</u>

Analysis:

Quantitative:

We used a multiple factor of 6 as given. We were able to find that the average ebitda valuation for the previous 3 years was $19.8 Million. However, do the recent decline, we also just calculated the 2024 amount which resulted in a valuation of $938K. This value is a significant decrease compared to the asking of $7.5 million for the company.

Some other considerations:

- Another valuation model may be better use for this example. the limitations are that it only focuses on income and expenses, which means it eliminates all of the companies assets such as inventory, PPE and cash. A better model would be Asset valuation, as it would consider all assets and liabilities, rather than just focusing on a single year of EBITDA.

Pro's:

- RJ's offers yoga and meditation studios, which supports CFL KSF of offering multiple services to clients. This meets that KSF.
- CFL currently does not have facilities in eastern Canada, by acquiring RJ's it will mean CFL becomes a nationwide Brand which will improve the brand recognition of CFL. This supports CFL KSF of Brand Recognition.
- By buying RJ's it will give CFL a total of 57 facilities (32+25). This will help overcome the weakness of being unable to secure funding. It was stated that companies need at least 50 studios before they would funded. this would give CFL 57 locations, which will allow them to apply for funding which would lead to additional funding for strategic options.

Con's:

- RJ's revenue and profit has severely decreased over the past 3 years. This is significant going concern question, which means it will likely file for bankruptcy if there is not a significant capital injection. This would be risky CFL to continue to invest capital into a company that has already tried many things to remain a float. The low revenues also severely decrease overall EBITDA which goes against what CFL wants to pursue.
- RJ's fitness machines has been stated as outdated, this goes against CFL's mission as it states that they provide State of the Art equipment. This does not agree with CFL's Mission.
- Staff members would be transferred to CFL. I will assume that since RJ's is going out of business, that the quality staff members have already been poached through competitors, this will leave the leftover staff. One of CFL's KSF is having high skilled and knowledgeable employees. If my assumption is correct, then this would go directly against that KSF.
- Similar to what CFL is facing, RJ would have to make the adjustment and focus on just one demographic, either <40, or >55. This means that RJ will be eliminate members from there gym. One of CFL's KSF is member retention, and by doing this is goes directly against that KSF.

Recommendation

I recommend that CFL does not pursue this option due to the fact the it will likely be going out of business here in the near future, it has decreased in revenues and profits over the past few years which goes against CFL's goal of growing EBITDA. It's EBITDA valuation is also for lower than what the offer to purchase is.

Other issues:

It was mentioned that with Rosa stepping back, CFL is looking for a new director to purchase her shares. The 2 options that were discussed were Louisa Rice and Albert Fong. I will discuss them, and recommend on one.

Lousia Rice:

- One of CFL's KSF is brand recognition through promotion, Louisa has a large following on social media. This means she would be able to promote the brand onto her existing fans which meets the KSF. This would result in new members as well which would increase the revenue and overall EBITDA.
- CFL's mission is to provide ever changing group classes, and Louisa is a teacher would be able to help unique fitness classes. This aligns with CFL's mission.
- She is a cross fit trainer with no formal experience in running a company. Rosa's role was the CFO of the company, which deals with budgeting, costs, and all other financial implications. By hiring Louisa, CFL would not have anyone to take over that role, which means they would have to a hire a new executive. This will increase wages, and lower overall EBITDA.

Albert Fong

- Albert has a background in corporate finance, which means he should be able to take over the CFO role from Rosa. I will assume that while he was in corporate finance, he had a vast experience in all things will fiance, which should cover most of what CFL is losing with Rosa's departure. This would also prevent CFL from hiring an executive to run the CFO position, which keeps wages down and increases EBITDA.
- He is also and expert in Pilates and yoga, this would be another service that CFL could incorporate into there facilities. This meets the KSF of providing multiple services to there members.
- He is based in Quebec, and CFL currently does not have facilities in Quebec, which means his research in fitness may differ from the markets in Western Canada. This could be a weakness as he would be unfamiliar with this new western market.

Recommendation

I recommend that CFL pursues Albert Fong as a shareholder due to his experience in corporate finance, he should be able to take over the CFO position of Rosa. He also is an expert in different group classes which matches CFL's of offering multiple service to members.

Overall Recommendation:

I recommend that CFL:

- Focus there attention to the >55 year old demographic and begin Specialising gyms to meet there needs. This is because they produce a higher EBITDA than the option which was CFL's main target, while only incurring $1 million in annual equipment investment as opposed to the $7 million. This option also aligns with CFL's corporate value of promoting health and fitness in local community, which is what the >55 demographic stated as its most important factor to the facility.

- Next I would sell off the contract of the Zenfit agreement for $9 million. This is because CFL will unlikely expand into Eastern due to not pursuing the RJ's purchase (discussed below), which means they will lose the contract for nothing into 2 years for nothing. As mentioned above, CFL will also begin focusing there attention on the >55 year old demographic which stated the machines were "very rarely, as the machines are too complicated to operate".

- Next, I would begin immediate construction on the new 6 rock climbing facilities with the cash CFL received from the sale of the Zenfit contract. This is due to option aligning with member retention, as all demographics have stated that they enjoy the rock-climbing facilities. It was also produces a substantial EBITDA of $2.2 million per year, and CFL has the majority of the market share, will it being stated there are no real competitors in the rock-climbing market.

- Finally I recommend that CFL does not pursue purchasing RJ's Health clubs limited. The averaging EBITDA valuation was greater than the investment, however the most recent annual EBITDA reflects a $7 million overvaluation. It is also has a going concern issue which mean it is decreasing in revenue and profit, which lowers EBITDA, which goes against what CFL is trying to pursue with EBITDA.

- Finally I would recommend Albert Fong to board of CFL due his corporate experience, he should be able to take Rosa's role as CFO. He also can prepare new group classes which meets CFL's mission of ever changing group classes.

Purpose: to find the EBITDA for both modernizing gyms and Specialinze Gyms over the next 3 years

Modernizing Gyms:

Members	2026	2027	2028	
<40	16281	24422	36632	
40-55	18318	20150	22165	
>55	2006	2006	2006	
total	36605	46578	60803	
Price	$550.00	$550.00	$550.00	
Total Revnue	20,132,750.00	25,617,900.00	33,441,650.00	
Personal traingin	11935800	11935800	11935800	
Total Revnue	32068550	37553700	45377450	
Wages	-20018250	-20018250	-20018250	
Other Expenses	-15359000	-15359000	-15359000	
	-35377250	-35377250	-35377250	
EBITDA	- 3,308,700.00	2,176,450.00	10,000,200.00	8,867,950.00

Specializing gyms

Members	2026	2027	2028		
<40	2171	2171	2171		
40-55	14988	13489	12140		
>55	12036	14443	17332		
total	29195	30103	31643		
Price	$650.00	$650.00	$650.00		
Total Revnue	18,976,750.00	19,566,950.00	20,567,950.00		
Personal traingin	13925100	14621355	15352422.75		
Total Revnue	32901850	34188305	35920372.75		
Wages	14298750	14298750	14298750		
Markettting	2500000	2500000	2500000		
Other costs	13573000	13573000	13573000		
	30371750	30371750	30371750		
EBITDA	2530100	3816555	5548622.75	11,895,277.75	
				3,027,327.75	differnece

Conclusion: Modernizing Gyms will produce and EBITDA of $8.8 million over 3 years while Specializing gyms will produce $11.9 million over 3 years

Purpose: to find the EBITDA for the Zenfit option

	2025	2026	
Units Sold	560.00	600.00	
Annual Sales	5,600,000.00	6,000,000.00	10000
Distributor Fee	840,000.00	900,000.00	
Less Related costs	50,000.00	50,000.00	
Annual Fee	790,000.00	850,000.00	
Subscribers	182,250.00	164,025.00	
Annual Views	2843100	2558790	**From prior years, each subscribes watches and average of 15.6 videos
	0.75	0.75	
Net	2,132,325.00	1,919,092.50	
EBITDA	2,922,325.00	2,769,092.50	

Conclusions: This option will produce a EBITDA of $2.9 million for 2025 and 2.7 million for 2026.

Purpose: to calculate the EBITDA of the 6 new proposed rock climbing studios

	2024
Number of Members	3920
8 Facilties	8
Member per Gym	490
Day Passes	2328480
Special Events	1345344
Other	1500576
total	5174400
Average	646800

	2025
Membership Fees/Facility	323400
Average Other Revenues	646800
Total Revenue/Gym	970,200.00
Total revenue	5,821,200.00

Expenses	2023	2024	Average	Per Gym
Wages	1,455,300.00	1,629,936.00	1,542,618.00	192,827.25
Purhcases	485,100.00	543,312.00	514,206.00	64,275.75
Marketting	207,900.00	232,848.00	220,374.00	27,546.75
OC costs	1,400,000.00	1,400,000.00	1,400,000.00	175,000.00
Other	1,039,500.00	1,164,240.00	1,101,870.00	137,733.75
				597,383.50

total Cost/gym on average	597383.5
total cost for 6 Gyms	3,584,301.00
EBITDA	2,236,899.00

conlusion: Opening the 6 new facilites will produce an EBITDA of $2.2 Million for 2025

Purpose: Calculate the EBITDA Valuation for RJs Health CLubs

	2022	2023		2024
EBITDA	6,624,640.00	3,133,982.00		156,384.00
Average Ebitda	3,305,002.00			
Multplie Factor	6			
EBITDA Valuation	19,830,012.00			
Sensitivity	2022	2023		2024
	6,624,640.00	3,133,982.00		156,384.00
Multplie Factor	6.00	6.00		6.00
EBITDA Valuation	39,747,840.00	18,803,892.00		938,304.00
Payment requirred	7,500,000.00			
Difference	32,247,840.00	11,303,892.00	-	7,037,280,000,000.00

Conclusion: the Valuation for the average past 3 years is $19.8 million, howver for the just the last year, it is $938K

APPENDIX E

THE COMMON FINAL EXAMINATION
DAY 1 CFL VERSION 2 BOOKLET – SEPTEMBER 12, 2023

COMMON FINAL EXAMINATION
SEPTEMBER 12, 2023 – DAY 1

<u>Case</u> (CFL-Version 2) (Suggested time: 240 minutes)

The date is May 1, 2025, and your boss at Serringers Consulting Group LLP (SCG) has assigned you, CPA, to another engagement with CanDo Fitness Ltd. (CFL).

Since SCG's engagement with CFL in 2022, CFL converted the eight fitness facilities identified by Brian into indoor climbing facilities. CFL also accepted Amanda's PurCafés proposal to open health food cafés within five of CFL's fitness facilities. So far, both investments have been successful. CFL decided against the acquisition of Mighty Fitness Inc. and did not proceed with the Zenfit proposal.

In order to make these investments, CFL accepted the sale-leaseback option from Hume Properties REIT (HPR) and cancelled the annual shareholder dividend of $2 million for 2022. The company has since resumed paying the annual dividend. CFL must also spend $4 million annually on new gym equipment to ensure that its fitness facilities stay up to date. In addition to these funds needed for the company's annual equipment purchases, CFL also has $6.5 million available for new investment projects but no access to further debt financing.

CFL successfully negotiated an agreement with its fitness instructors, increasing their compensation, and paying them fairly for all hours worked (including the time it takes to prepare, set up, and take down any equipment required for the class). The quality of fitness classes has therefore improved, resulting in greater member satisfaction and increased member retention.

Given the success of the PurCafés and climbing wall initiatives, the Board of Directors (the board) is eager to make investments to further diversify CFL's sources of revenue. For any strategic investments made, the board wishes to increase both CFL's revenue and EBITDA. However, given the desire to protect the company's dividend, the board will give preference to less risky projects that are simple to operate and that provide a stable and reliable source of revenue.

In late 2022, the company's vision and mission statements were updated and are currently as follows:

Vision statement: *To provide equipment, classes, and other amenities and services in a friendly and welcoming atmosphere to motivate and help individuals to achieve a healthy lifestyle.*

Mission statement: *To provide the means for people of all ages to embrace a fit and healthy lifestyle, providing state-of-the-art equipment and innovative, fun, and challenging group classes.*

In recent years, the popularity of healthy lifestyle choices has grown considerably, resulting in a significantly higher demand for fitness products and services. Products and services that provide the convenience of working out at home have become particularly popular, and the demand for nutritious food options has grown steadily.

In January of this year, to support the desire for improved health, the Government of Canada unveiled a new Fitness Rebate Program (FRP), which provides a tax credit of up to $750 per year to all Canadians who purchase products and services directly related to exercising.

The board has asked you to review the information provided and prepare a report that strategically analyzes and makes a recommendation for each potential investment option. You are also to advise the board of any significant factors that have not been considered. The board would also like you to comment on CFL's overall strategic direction and on how each proposal could influence that direction. For this engagement, please ignore any corporate tax implications within your analysis and recommendations.

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APPENDIX I
BOARD MEETING WITH CPA IN ATTENDANCE

May 1, 2025

Phillip: Thank you for joining us, CPA.

I am happy to say that CFL's financial situation has improved since our last engagement with SCG. We mainly attribute this to our improved annual membership retention rates and to the additional revenue generated from our climbing walls and PurCafés.

Rosa: CPA, we should also mention that we have begun discussing reducing our involvement in the day-to-day operations of CFL. Although a firm date has not been set, the intention is to remain as board members, but to entirely hand over CFL's management functions to the company's senior managers in roughly five years.

Phillip: Good point, Rosa. CPA, once we are not actively managing operations, we will no longer take a salary, and will instead rely on the dividends we receive from CFL to fund our retirements.

CPA: Noted.

Phillip: Great. Frank, please introduce the first investment option.

Frank: Iron Depot has recently been put up for sale, for $10 million. It sells both new and used exercise equipment at reduced prices. There are currently nine Iron Depot outlets, located in Victoria, Vancouver, Edmonton, Calgary, Saskatoon, Winnipeg, Ottawa, Quebec City, and Halifax.

Rosa: We do not have enough available investment capital for this, Frank.

Frank: Thankfully, that does not preclude this option. The current owner of Iron Depot is willing to provide a $7.5 million loan to the purchaser, so we would only need to pay $2.5 million in upfront cash.

Sandra: Although diversifying our revenue sources is important to the board, it concerns me that Iron Depot's business is significantly different from anything we have done before. What else can you tell us about Iron Depot?

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

May 1, 2025

Frank: The company began nearly 25 years ago with an outlet in Victoria. Since then, it has gradually opened new locations across the country. The Halifax location is the newest, having opened in 2021. To date, only one Iron Depot outlet, located in North Bay, Ontario, has had to close. According to our due diligence, the population of North Bay, at just over 50,000 people, was too small to support an exercise equipment retailer. Most of Iron Depot's customers are fitness facilities similar to CFL, and individuals who want exercise equipment at home.

Phillip: If we buy it, who will manage the nine outlets? Will Iron Depot's current management team stay on board after the sale?

Frank: Unfortunately, the current owner, who takes an active approach in the company's management, wants to retire completely after the sale. We would need to hire a senior manager to oversee the operations. However, Iron Depot's business model is quite basic. The most important contributors to the company's success are three main supplier contracts, which provide Iron Depot with wholesale prices on equipment. Each of these contracts has recently been locked in for at least another 10 years.

Rosa: Companies similar to Iron Depot have recently sold at a price equal to 4.5 times their EBITDA. Frank, tell us more about the supplier contracts. Given that CFL could buy equipment at wholesale prices, what discount would we get on our future equipment purchases, compared to what we currently pay?

Frank: At least 20%. These supplier contracts could also be used for purchases beyond Iron Depot's inventory.

Phillip: Thank you. Sandra, you are next.

Sandra: Thanks, Phillip. Sunnyside Hotels (Sunnyside) wants to capitalize on the current popularity of health and fitness by opening a small, but well-equipped, gym in each of its seven hotels. As Sunnyside has no experience in this area, it approached CFL to see whether we would be interested in signing a management contract for the hotel gyms.

As part of Sunnyside's current proposal, CFL would be responsible for designing and operating each hotel gym, and for providing the necessary equipment. CFL would retain ownership of the equipment installed in the hotel gyms. In return, Sunnyside would pay CFL a fixed amount each year.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

May 1, 2025

Frank: It will be a challenge to design the gyms, especially because we have limited space within each hotel. After the gyms open, what other responsibilities would CFL have?

Sandra: CFL would provide the staff necessary to operate each hotel gym and maintain the equipment. CFL will also be required to provide new equipment every two years. Sunnyside has proposed calling the hotel gyms "Sunnyside Gyms by CanDo Fitness."

Brian: I like the fact that CFL would get free marketing through this arrangement. We might be able to convert some hotel guests into members of CFL's gyms.

Phillip: Yes, but what happens if something goes wrong or someone gets hurt in a hotel gym?

Rosa: And how much will it cost to buy all the necessary equipment?

Sandra: Prior to today's meeting, I had Frank compile a rough estimate. Based on conversations with one of CFL's existing suppliers, he estimates that it will cost a total of approximately $650,000 to provide all seven hotel gyms with new equipment.

Phillip: Thanks, Sandra. Brian, you are next.

Brian: Okay. Through my friends in the film industry, I was introduced to Rise Edustream (RiseEd), which is a company that produces and distributes educational videos. RiseEd has offered CFL the opportunity to use their services in order to create fitness videos for an online platform.

Phillip: This sounds like the video-streaming component of the Zenfit proposal we assessed in 2022.

Brian: That's right, Phillip. The concept is the same; however, in this case, the videos would use our brand instead of Zenfit's. Because of that, CFL could receive a great amount of exposure to a new potential client base. We would also be in complete creative control regarding the type of videos we release. Strength, cardio, yoga, meditation, you name it—we could create an extensive catalogue of fitness videos that our subscribers could use at home.

Rosa: What will it cost? And what role will RiseEd play?

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

May 1, 2025

Brian: RiseEd will charge us a fee based on the number of subscribers that we attract to the platform. For each 10,000 subscribers or part thereof, RiseEd will charge us $2 million annually. For example, if at the end of the year, we have 2,500 subscribers, RiseEd will charge us $2 million for that year. If at the end of the next year, we have 21,000 subscribers, RiseEd will charge $6 million for that year.

RiseEd will look after the technology component, such as the online platform that our subscribers will use to access the videos. RiseEd will also produce the videos. CFL will only need to provide the fitness instructors and workout programs, and will be responsible for marketing the product and providing its subscribers with customer support.

Rosa: What about startup costs?

Brian: RiseEd estimates a cost of $2.5 million for CFL, of which $1.5 million will go to RiseEd in order to create the online platform. The other $1 million will go toward the development of a filming studio and purchasing the equipment necessary to videotape the workouts.

Phillip: I am not sure, Brian. When we researched video streaming as part of the Zenfit proposal, we discovered many other competitor products, and that was over three years ago! How confident are you about the number of subscribers that RiseEd has projected for each year?

Brian: We would need to increase our marketing budget and the effort we put into our presence on social media. That initiative, combined with using the perfect instructors to lead the workouts, would strongly contribute to the number of subscribers that we will attract to the platform. We could also hire a few professional athletes to promote, and possibly even participate in, the fitness videos we offer.

Phillip: Interesting idea. Lastly, we have identified eight CFL fitness facilities that have underutilized space, which could be used to generate additional revenue. We have two alternatives that we want to consider for the surplus space. Rosa, please tell us about the potential physiotherapy clinics.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

May 1, 2025

Rosa: As we know, exercise and fitness have never been more popular. One consequence of this trend is that more people are suffering from exercise-related injuries. Given this, the demand for physiotherapy services is increasing. I was recently presented with an opportunity from one of our long-term gym members, Nav Srinivasan, a highly experienced physiotherapist. He has offered to oversee the development and operation of eight new CFL physiotherapy clinics. Based on my research, each clinic will cost $495,000 to renovate and equip (equipment costs represent 70% of the initial $495,000).

Sandra: Have we identified the key success factors of this project?

Rosa: The quality of our therapists is critical. Once we have secured a team of highly qualified physiotherapists, we would then need to market our clinics aggressively. As well, the reputation of a clinic is critical for its success. We therefore need to ensure that our customers have a good experience.

Brian: Physiotherapy is very different from CFL's current offerings. We would essentially be starting from scratch. We would need to launch a new website for this service.

Rosa: We would also need to secure comprehensive insurance coverage. However, once the clinics reach full utilization, the profitability of the project is undeniable. This is a highly specialized and technical service, and the revenue potential is very attractive.

Frank: Would the clinics' customers be able to use the new FRP government rebate?

Rosa: Not currently. However, the government has indicated that it may revise the program's guidelines to include physiotherapy in the future.

Phillip: Offering our members these services directly within our gyms would be a competitive advantage for us. It may help us attract and retain members. Sandra, please tell us about the other alternative.

Sandra: Okay. Amanda would like to expand our PurCafés arrangement by opening a new café in each one of the gyms that has underutilized space. Each new café will cost $340,000 in renovations. If we accept the proposal, Amanda's compensation will increase to 20% of PurCafés' net operating profit.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

May 1, 2025

Phillip: Amanda has certainly proven herself. We have received excellent feedback from our first five cafés, and our members love having easy access to tasty and nutritious food.

Rosa: Although that is true, the revenue potential for these cafés is far below that of the physiotherapy clinics. As well, Amanda has been making decisions on her own lately. For example, she altered several menu items without discussing that change with us first. That is a worrying trend.

Sandra: I also question Amanda's workload. Since 2022, she has opened three more of her own vegetarian restaurants, and now wants to open eight more PurCafés? That seems like a lot. With all that Amanda has going on, I am concerned that the quality of our PurCafés will decline.

Frank: Amanda has been a pleasure to work with and has helped create value for CFL. With the original five PurCafés, the initial renovation was certainly a logistical challenge, but once they opened for business, the board's involvement in the operations of the cafés has been minimal. Amanda has taken the lead at every step.

Sandra: And finally, the trend toward healthy lifestyles has attracted many new entrants into the market. There are now far more restaurants and cafés that offer healthy choices when compared to three years ago.

Phillip: Good point, Sandra. Thank you all for your contribution today. CPA, the board looks forward to your report. Meeting adjourned.

APPENDIX II
IRON DEPOT

Prepared by Frank Chang

Since its inception, Iron Depot's revenue growth has been driven mainly by the opening of new outlets. Each current outlet has one manager, and a few staff members who help answer customer questions.

Financial Details

Iron Depot
Income Statement
For the year ended December 31, 2024
Audited

Revenue	$ 18,720,200
Expenses	
Purchases	10,296,100
Wages	2,550,400
Occupancy costs	1,928,600
Marketing and advertising	950,100
General and administrative	827,200
Total expenses	16,552,400
Operating income	2,167,800
Less: interest expense	91,800
Income before taxes	$ 2,076,000

Included in general and administrative expenses is a one-time, $450,000 expense incurred to hire an investment bank and accounting firm, to help Iron Depot with the sale of the company.

Included in wages is the owner's salary of $75,000. CFL will likely pay the senior manager, who will replace the owner, a salary of $115,000 per year.

As of December 31, 2024, Iron Depot had the following:

- A cash balance of $10,000
- An outstanding interest-bearing debt balance of $1.4 million

APPENDIX III
SUNNYSIDE HOTELS GYM MANAGEMENT CONTRACT

Prepared by Sandra MacCarthy

Sunnyside will compensate CFL $1.85 million for each year of the contract.

The initial term of the contract will be five years, and will be extended for an additional five years if Sunnyside's guests are satisfied with the gyms.

Sunnyside expects the gyms to open on January 1, 2026. Each gym will be open from 6:00 am to 10:00 pm, 365 days per year. As part of the contract, Sunnyside requires each hotel gym to always have one CFL staff member present during opening hours. These staff members will be expected to answer questions that the gyms' users may have, and to ensure that the equipment is well maintained. CFL will pay these staff members $20 per hour. CFL will also need to hire a new senior manager to oversee the gym operations within Sunnyside's hotels, at a salary of $115,000 per year.

The salvage value of the used equipment will be approximately 40%. The cost of capital for this project is 12%.

APPENDIX IV
STREAMING FITNESS CLASSES

Prepared by Brian Mitchell

The audience for streaming fitness videos has grown quickly. A recent industry report indicated that this trend is expected to continue for the foreseeable future. Other fitness companies have been able to secure a loyal base of subscribers through pairing their streaming videos with a unique piece of exercise equipment, such as Zenfit's Zentracker exercise machine. In discussions with RiseEd, they mentioned the exciting possibility of CFL developing its own piece of unique equipment at some point in the future.

RiseEd provided the following projection for the project's first three years. All expenses are fixed, other than RiseEd's fee, which will increase with each additional 10,000 subscribers (or part thereof).

	2026	**2027**	**2028**
Number of subscribers	10,000	25,000	35,000
Subscription cost (monthly fee)	$40	$40	$40
Monthly revenue	$400,000	$1,000,000	$1,400,000
Annual revenue	$4,800,000	$12,000,000	$16,800,000
Expenses			
Fee to RiseEd	2,000,000	6,000,000	8,000,000
Labour	750,000	750,000	750,000
Marketing	500,000	250,000	250,000
General and administrative	45,000	45,000	45,000
Total expenses	3,295,000	7,045,000	9,045,000
Operating income	$1,505,000	$4,955,000	$7,755,000

RiseEd has proposed that the agreement have an initial term of six years, with a renewal option at CFL's discretion for a further six years.

APPENDIX V
PHYSIOTHERAPY CLINICS

Prepared by Rosa van der Schuren

Financial Projections and underlying assumptions

- Each physiotherapy clinic will be open from Monday to Friday from 9:00 am to 5:00 pm for 48 weeks each year.
- Each clinic will have a waiting room and four private examination rooms.
- If the eight clinics can achieve 100% utilization, revenue is projected to be $6,720,000. At 75% and 50% utilization, revenue would equal $5,040,000 and $3,360,000, respectively.
- Operating costs are expected to be as follows:
  - Variable costs will equal 20% of revenue.
  - Each clinic will employ four physiotherapists, at an annual salary of $90,000 each.
  - Other fixed costs are expected to be $105,000 per clinic per year. Amortization is included in this amount (each clinic's equipment is expected to have a 10-year life).
- Not included in the above expenses is Nav's requested annual salary of $250,000, to lead the development and operation of the new clinics.

Additional Project Details

- For accessibility reasons, each gym with a physiotherapy clinic will require parking spots to be dedicated to the clinic in front of the gym.
- Lenders have a favourable perception of healthcare-related clinics that have achieved stable revenue. These clinics can often access debt financing at favourable rates.
- Patients who are satisfied with the treatment they receive appear to be highly loyal to their physiotherapy clinic.

APPENDIX VI
OPENING OF NEW PURCAFÉS

Prepared by Sandra MacCarthy

The following internally-generated earnings report details the average performance of a PurCafé. The report was compiled using data from CFL's existing five PurCafés.

PurCafés
Earnings Report (per café average)
For the year ended December 31, 2024

Revenue	$ 896,400
Expenses	
Variable cost of food and beverages	421,300
Labour	131,000
Supplies and other costs	50,000
Amortization	39,000
Advertising	11,000
Total expenses	652,300
Operating profit	244,100
Amanda's portion (15%)	(36,600)
Net operating profit to CFL	207,500
Number of PurCafé locations	5
Total operating profit to CFL	$ 1,037,500

Currently, 80% of the PurCafé revenue is generated from CFL members who eat in the café after a workout; the other 20% is from non-members who only come into the gym to use the café. Since the introduction of the first five cafés, membership retention rates at the fitness facilities that include a PurCafé have improved. Members have also commented that the cafés have helped to strengthen the community atmosphere of the gyms. However, throughout this year, CFL has received several comments from gym members, who say that the quality of service at the cafés has declined lately. One member also mentioned that, for the first time since their gym's café opened, certain menu items were unavailable to order.

To supply the proposed eight new PurCafés, Amanda plans to lease two additional locations that will be used to process the food before it is ready for the cafés. The annual lease expense will be $225,000 for each location. Aside from this new expense, Amanda expects that the revenue and costs for each new PurCafé will be very comparable to the average performance of the existing PurCafés.

APPENDIX F

DAY 1 (CFL VERSION 2) – SEPTEMBER 12, 2023
MARKING GUIDE AND SAMPLE CANDIDATE RESPONSE

MARKING GUIDE
CANDO FITNESS LIMITED (CFL)
VERSION 2

Summative Assessment #1 – Situational Analysis

For Summative Assessment #1, the candidate must be assessed for reasonableness of attempt:

Yes – The candidate used a reasonable situational analysis when analyzing the major issues facing CFL.

Unsure – The candidate attempted to use a reasonable situational analysis when analyzing the major issues facing CFL.

No – The candidate clearly did not use a reasonable situational analysis when analyzing the major issues facing CFL.

Based on the 2022 Competency Map:

Technical Competency
2.3.2 Evaluates the entity's internal and external environment and its impact on strategy development

Enabling Competencies
1.4.1 Performs work carefully, thoroughly and competently in accordance with relevant technical and professional standards
2.1.1 Applies knowledge of the organization's competitive environment and strategic direction when performing assigned work
2.1.3 Identifies the strategic impact of internal decisions and external influences on project plans and initiatives
6.1.1 Identifies and articulates issues within areas of work responsibility
6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

The candidate is expected to complete an appropriate situational analysis.

The focus should be on describing the factors that have changed since Capstone 1 that will affect the decisions at hand. Recapping parts of the mission/vision and relevant KSFs, and presenting relevant elements of the SWOT, is appropriate.

The candidate should draw upon their situational analysis when analyzing CFL's opportunities (purchase Iron Depot, design/manage Sunnyside Hotel gyms, produce and stream fitness videos online, and either open physiotherapy clinics or open new PurCafés in gyms that have available space).

Vision/Mission

In late 2022, the company's vision and mission statements were updated.

Vision statement: *"To provide equipment, classes, and other amenities and services in a friendly and welcoming atmosphere to motivate and help individuals to achieve a healthy lifestyle."*

Mission statement: *"To provide the means for people of all ages to embrace a fit and healthy lifestyle, providing state-of-the-art equipment and innovative, fun, and challenging group classes."*

CFL has five main core values, also approved by the Board of Directors in 2017, as follows:

1. All employees are caring and understanding of members and work as part of a team to meet the corporate goals and mission. Members, guests, and staff are treated with honesty, dignity, and respect at all times.
2. We continuously update our equipment to ensure that it is leading edge, and provide ever-changing group classes that stay up to date with the current trends. We provide unmatched service by having uniquely qualified and passionate staff.
3. All staff are committed to their own fitness goals and healthy living and are able to motivate members to do the same.
4. We strive to build a community of friends in a safe and supportive environment and to be a driving and vocal force in the local community to promote fitness and healthy living.
5. We provide activities that are fun, challenging, and designed to help individuals achieve their fitness goals.

New Objectives

At the May 1, 2025, board meeting, the following objectives were set:

- Increase the company's revenue and EBITDA.
- Reduce the risk of any investments made in order to protect the company's annual dividend payment. (The board members have begun to discuss their plan to eventually retire and therefore step back from the day-to-day operations of the company within five years.)

Shareholder Preferences

For any strategic investments that are made, the board will give preference to the alternatives that:

- help the company further diversify its revenue sources;
- are simple to operate; and
- provide a stable and reliable source of income.

Available Cash Flow /Financing

At present, CFL has $6.5 million available for investment, and no access to further debt financing through its bank. In addition to this amount, CFL must spend $4 million annually on new gym equipment. Further, CFL's directors want to ensure that the company's $2 million annual dividend is both protected and paid.

Candidates are NOT expected to recap KSFs or do a SWOT in detail. However, they must draw upon these in their analysis of the strategic options presented.

Key Success Factors (KSFs)

KSFs in the gym, health, and fitness facility (fitness) industry in Canada include the following:

- Easy access for clients – the facility should be located as close as possible to its members.
- Effective promotion of products and services – the more brand awareness that a facility has, the more members it will attract.
- Offering a wide range of services and multiple locations – this will help attract new members and retain existing members.
- Providing clean facilities with good-quality equipment.
- Providing good customer service.
- Having skilled (trained) employees – employees should be both knowledgeable and friendly/motivational.
- Retaining members – it is usually more costly to bring in new members than to retain existing members.

- Innovation – to be successful, a company in the fitness industry must research and stay up to date with the current trends.

SWOT Analysis

Strengths:

- CFL has been able to diversify its revenue stream with the addition of the indoor climbing facilities and PurCafés investments – this means that the company's performance is less dependent on the number of fitness gym members.
- CFL was able to successfully negotiate an agreement with the company's disgruntled fitness instructors. Now that the fitness instructors are more fairly compensated, the quality of CFL's fitness classes has improved, which has led to an improvement in the company's member retention rate and overall member satisfaction.
- CFL's financial situation has improved – this is a result of the company's investments in the indoor climbing walls and PurCafés, and to an improvement in membership retention rates. The company is in a position to expand on this success by making further investments within the industry.

Weaknesses:

- CFL does not have any further access to debt financing and will therefore be limited by its available cash resources relative to the investment options that it can proceed with.
- CFL's board members plan to retire from active involvement in the company's day-to-day operations in approximately five years – this means that the company will need to find the right personnel to replace them, to ensure that the company continues to operate effectively.

Opportunities:

- The popularity of healthy lifestyle choices has grown considerably – this has led to an increase in the demand for products and services related to fitness. CFL can take advantage of this increase in demand by expanding the number of products and services it offers.
- Home workouts have become particularly popular – if CFL can find viable investments that allow customers to work out from home, the company could take advantage of this growth in popularity.
- Given the increase in healthy lifestyle choices, the demand for nutritious food options has also grown – CFL could take advantage of this growth in demand by opening more PurCafés, an investment option that has recently become available.

- The Government of Canada introduced a new fitness rebate program (FRP) at the beginning of the current year. The FRP gives each individual an annual $750 tax credit for purchases that relate directly to products and services used to exercise. CFL could take advantage of this by offering more products and services that are eligible for this tax credit.
- Iron Depot, an exercise equipment wholesaler, has come up for sale – CFL could purchase it and diversify its revenue into equipment sales. This option offers an attractive discount on equipment purchases that CFL could use to lower its cost of equipment purchases.
- Sunnyside Hotels (Sunnyside) wants CFL to design and manage gyms within its hotels. This opportunity would allow CFL to diversify its revenue with a stable, fixed-income contract.
- Rise Edustream (RiseEd) has offered CFL its services to create and distribute online fitness videos. This type of product could provide CFL with a significant boost in revenue, as well as brand awareness, and allow CFL to tap into the home-workout market.
- CFL has identified eight of its current fitness facilities that have underutilized space, which could be used to generate income. There are two options currently available in relation to the underutilized space: open physiotherapy clinics, or PurCafés, in each of the eight gyms.

Threats:

- The board stated that protecting the company’s annual dividend payment is an important consideration, given their plans to retire (as managers) in roughly five years. If any of the investments made do not provide a suitable and stable return, that could jeopardize the security of the dividend payment.
- By choosing to focus on making investments outside of their traditional business of acquiring and retaining members at its fitness facilities, the board is risking a loss of focus on the company’s main revenue source. Although diversifying revenue sources is a good way to reduce risk, the board needs to ensure that an adequate amount of attention is given to CFL’s core business.

Conclusion

After a period of improved performance, CFL's board is eager to continue to diversify the company's revenue streams into areas outside of annual membership fees. The company has several investment opportunities, and the objective to reduce risk as much as possible while also increasing its revenue and EBITDA. If the company's investment capital is used in an effective way, the shareholders will more likely be able to retire with the confidence that the company's annual dividend is likely to continue. Therefore, it is crucial to evaluate each investment opportunity, to determine which ones provide the highest return while not increasing risk to a level that might jeopardize the company's ability to issue the board dividends.

Summative Assessment #2 – Analyzes the Major Issues

For Summative Assessment #2, the candidate must be assessed for reasonableness of attempt:

Yes – The candidate sufficiently completed a reasonable assessment of the major issues facing CFL.

Unsure – The candidate attempted to complete a reasonable assessment of the major issues facing CFL.

No – The candidate clearly did not complete a reasonable assessment of the major issues facing CFL.

Technical Competency
2.3.3 Evaluates strategic alternatives

Enabling Competencies
1.1.3 Exhibits ethical behavior by complying with laws and regulations, organizational policies, societal norms and personal ideals
6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems
6.1.3 Demonstrates skepticism, objectivity, due care and persistence when identifying issues
6.2.3 Questions the relevance and tests the quality of information and assumptions in own analyses
6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

This summative assessment is based on Assessment Opportunities #2 to #6.

Assessment Opportunity #2 (Strategic Issue #1 – Acquire Iron Depot?)

The candidate is expected to complete both a quantitative and qualitative assessment of whether CFL should acquire Iron Depot.

Quantitative analysis: The candidate should calculate the value of Iron Depot and compare that figure to the asking price. The candidate should also assess the impact that acquiring Iron Depot would have on CFL's revenue and EBITDA.

Qualitative analysis: The candidate should discuss the advantages and disadvantages of this investment opportunity. Particular attention should be paid to the risks associated with the investment, and whether the board's objectives/preferences would be satisfied.

Conclusion: The candidate should offer a conclusion that incorporates and logically follows from their quantitative and qualitative analyses.

Iron Depot is an exercise equipment wholesaler that sells both new and used products. There are currently nine Iron Depot outlets located in major cities throughout Canada. Iron Depot is for sale for an asking price of $10 million. The current owner is willing to provide a $7.5 million loan with the purchase. Therefore, the initial upfront cash required to proceed with this strategic alternative is $2.5 million.

Quantitative Analysis

<u>Normalized EBITDA calculation:</u>

Operating income	**$**	**2,167,800**
Adjustment for owner's salary ($115,000 - $75,000)		(40,000)
Consultant fees		450,000
Normalized EBITDA		2,577,800
EBITDA multiple		4.5
Enterprise value		11,600,100
Less: interest-bearing debt outstanding, net of cash		(1,390,000)
Equity value	$	10,210,100

The implied equity value of Iron Depot is $10.2 million, which is slightly greater than the current asking price of $10 million. Therefore, it appears that the asking price is reasonable.

However, there are additional considerations that CFL should factor into the decision:

- Iron Depot's supplier contracts will allow CFL to purchase its equipment at wholesale prices. According to Frank, this discount will be at least 20%. Given that these contracts can be used to make purchases beyond Iron Depot's inventory, this aspect of the Iron Depot proposal represents a major synergy between this option and CFL's main operation – the fitness gyms. Each year, CFL spends approximately $4 million on new gym equipment. With the supplier contracts that come with the Iron Depot acquisition, CFL would save approximately $800,000 annually on the purchases the company makes to ensure that its gym equipment remains up to date.
- One of the board's stated objectives is to increase the company's revenue and EBITDA figures. Based on the analysis above, this investment opportunity would help to accomplish this objective – if CFL decides to invest in Iron Depot, the company's EBITDA will increase by approximately $2.5 million annually.
- The FRP will allow each Canadian citizen to use up to $750 worth of fitness and services purchases as a tax credit. This incentive program will likely increase the revenue of companies that provide products and services that are eligible for the rebate. Therefore, Iron Depot's revenues are likely to increase because of the FRP incentivizing people to exercise. This increase has not been factored into the analysis above.
- The details of the $7.5 million loan that Iron Depot's current owner will extend to CFL were not included in the information that Frank provided in Appendix II. Before an investment decision can be made, CFL needs to obtain and analyze these details, to ensure that the terms are reasonable, and that any interest costs are built into the EBITDA estimate.
- Prior to finalizing the offer to Iron Depot, CFL may also want to engage a third-party business valuator to ensure that the assumptions used in the calculation above, such as the EBITDA multiplier, are appropriate, given current market conditions.
- Although the current owner of Iron Depot appears to be entering retirement, CFL may want to consider adding a noncompete clause to the purchase agreement, to ensure that the old owner does not create a new competitor business to Iron Depot.

From a quantitative perspective, the investment in Iron Depot is very attractive. Not only is the value of the company greater than its asking price, but there is also a significant synergy between this option and CFL's core business. This investment option satisfies the board's objectives and offers significant advantages.

Qualitative Analysis

Advantages:

- Iron Depot sells used equipment – this may allow CFL to dispose of its used equipment in a more effective way, which could save time and money. This vertical integration may offer CFL significant benefits now and in the future.
- Iron Depot’s business appears to be quite stable. Only one out of ten Iron Depot outlets has needed to close (the North Bay outlet closed due to the city’s smaller population). The shareholders expressed a preference for investing in projects that offer stable and secure revenue. This opportunity appears to satisfy this preference.
- Iron Depot expanded into Halifax in 2021, which demonstrates that Iron Depot is still growing. It is possible that CFL could further expand Iron Depot’s operations after acquiring the business.
- The FRP may represent a big opportunity for Iron Depot to further expand its operations into other cities with enough of a population to support an Iron Depot outlet – this is because the amount of dollars spent on fitness products and services is likely to increase because of the government tax incentive.
- The asking price of Iron Depot is $10 million, which is more than CFL currently has available for investment – however, Iron Depot’s owner is willing to provide the purchaser with a $7.5 million loan. This loan will enable CFL to make the purchase without depleting its available cash resources.
- Iron Depot’s business generates income by selling new and used gym equipment. Therefore, this investment would help CFL satisfy its objective of diversifying revenue.
- Iron Depot is 25 years old and extends all over Canada – this historic success should provide at least some confidence to CFL’s board that Iron Depot’s business is stable and secure – an important consideration, given the board’s objective to protect the company’s annual dividend.
- The most important contributor to Iron Depot’s success is its main supplier contracts, which were recently locked in for at least 10 years. This means that Iron Depot’s current low-cost equipment supplies will continue.
- Iron Depot has a basic business model. This likely means that the business is relatively simple to operate – this aligns with the shareholders’ preference to invest in businesses that are easy to operate.
- One of Iron Depot’s main customer segments is individuals who want to exercise at home – therefore, the purchase of Iron Depot aligns with the industry trend of home workouts becoming more popular.

<u>Disadvantages:</u>

- CFL's board does not have any experience in selling wholesale gym equipment – therefore, the performance of Iron Depot may suffer during the time in which CFL learns how to best operate the business.
- Iron Depot's owner intends to retire after the business is sold – therefore, the expertise of the current owner relative to the business's operations will be lost. This represents a significant risk to the investment, given that CFL has no experience in selling wholesale gym equipment.
- To replace the owner, CFL intends to hire a senior manager to oversee operations – this represents a risk, given that it is uncertain whether the new hire will perform effectively. To mitigate this risk, CFL may want to allocate one of its board members to oversee the operations of Iron Depot, especially in the first year or two of ownership.
- Iron Depot has locked in its three main supplier contracts for the next 10 years – this means that CFL will have limited flexibility in terms of which suppliers the company can use. CFL should perform research to ensure that these suppliers are suitable, and will provide the type of quality that CFL's members expect.

Conclusion

Both qualitatively and quantitively, this investment satisfies the board's objectives without adding a significant amount of risk to CFL's business. The actual earnings of Iron Depot plus the synergies that the business would offer CFL's existing businesses make this strategic alternative very attractive. CFL should still perform an adequate level of due diligence, to ensure that the analysis above is realistic. If CFL determines that the analysis performed here is reasonable, it should make the investment.

Assessment Opportunity #3 (Strategic Issue #2 – Design and manage Sunnyside Hotel gyms?)

The candidate is expected to complete both a quantitative and qualitative assessment of whether CFL should accept the contract with Sunnyside to design and manage the hotel gyms.

Quantitative analysis: The candidate should calculate the profitability of the contract, and should also discuss whether the contract aligns with the board's objectives to increase CFL's revenue and EBITDA.

Qualitative analysis: The candidate should discuss the advantages and disadvantages of this investment opportunity. Particular attention should be paid to the risks associated with the investment, and whether the board's objectives/preferences would be satisfied through this option.

Conclusion: The candidate should offer a conclusion that incorporates and logically follows from their quantitative and qualitative analyses.

Sunnyside Hotels (Sunnyside) wants CFL to design and manage seven hotel gyms within Sunnyside's current hotels. Sunnyside will pay CFL $1.85 million per year for the management contract, which has an initial term of five years and the potential for an additional five-year extension.

Quantitative Analysis

Cash flow projection – if contract lasts for five years:

Year	**0**	**1**	**2**	**3**	**4**	**5**
	$	$	$	$	$	$
Annual payment from Sunnyside		1,850,000	1,850,000	1,850,000	1,850,000	1,850,000
Salary expense – senior manager		(115,000)	(115,000)	(115,000)	(115,000)	(115,000)
Salary expense – onsite employee		(817,600)	(817,600)	(817,600)	(817,600)	(817,600)
Equipment purchase	(650,000)		(650,000)		(650,000)	
Equipment salvage value (40%)			260,000		260,000	260,000
Total cash flow	(650,000)	917,400	527,400	917,400	527,400	1,177,400
NPV factor (@ 12%)		0.8929	0.7972	0.7118	0.6355	0.5674
Present value of future cash flows	(650,000)	819,146	420,443	653,005	335,163	668,057
Net present value of management contract	2,245,815					

Based on the information provided, the management contract with Sunnyside represents over $2.2 million of present value to CFL. This amount could also increase if Sunnyside decides to expand its operations and requires CFL to manage more of its hotel gyms. The above projection assumes that the contract would end after five years; however, it is also possible that the contract's terms would be extended. If the contract is extended, it would become more quantitatively attractive for CFL. The above projection also assumes that the salvage value of the gym equipment used in the hotel gyms would equal 40% at the end of Year 5. However, the salvage value may increase, given that the equipment would only be one year old.

In addition, there would be a valuable synergy between this strategic option and the option to purchase Iron Depot. The above analysis does not include the 20% discount on equipment purchases that CFL would gain if the company acquires Iron Depot. Therefore, if CFL decides to both purchase Iron Depot and sign the management contract with Sunnyside, the above results will be improved *(integration)*. CFL currently has enough investment capital available to proceed with both options.

From a quantitative perspective, the management contract with Sunnyside appears to be an attractive opportunity.

Qualitative Analysis

Advantages:

- CFL can leverage its core competency (operating gyms) to generate further revenue. In addition, because CFL does not currently generate revenue through hotel gyms, this opportunity would allow CFL to diversify its revenue sources.
- The responsibilities that CFL would have under the management agreement all align with areas where CFL has a large amount of experience – therefore, the risk that CFL would be unable to effectively carry out the contract is likely to be low.
- Sunnyside will pay CFL a fixed amount each year – this represents a stable and secure new source of revenue. This aligns very well with the preferences of CFL's shareholders.
- Once built, operating the hotel gyms seems very straightforward and simple. CFL will only need to ensure that one CFL staff member is on hand while the hotel gyms are open each day. This simplicity aligns well with the investment preferences of the shareholders.
- CFL's main business, the fitness facilities, may benefit from this management contract because of the free publicity that the company would derive from this proposal (Sunnyside proposes to call the hotel gyms "Sunnyside Gyms by CanDo Fitness"). The effective promotion of products and services is a key success factor within the fitness industry.

Disadvantages:

- Frank stated that it would be a challenge to design and build the gyms – as Sunnyside wants to open the hotel gyms on January 1, 2026, which is less than one year away, this factor is likely to be made even more challenging. CFL should ensure that this timeline is realistic – especially given that the company may enter into other new projects at the same time (such as the purchase of Iron Depot and the decision on how best to use the additional space at the eight fitness gyms).

- CFL will retain ownership of the gym equipment used in the hotel gyms, and this equipment needs to be replaced every two years – this will increase the logistical challenges of this option, given that CFL will need to both buy and sell new equipment for the gyms every two years.
- As Phillip pointed out, what happens if someone gets injured in one of Sunnyside's hotel gyms? Which company would be held liable, Sunnyside or CFL? This aspect of the proposal is currently unclear. To ensure that CFL is protected from any potentially costly lawsuits, an adequate level of insurance should be purchased. The party, either Sunnyside or CFL, that will bear the responsibility for ensuring the safety of the gym's users also needs to be clarified.
- The term of the contract will only be extended if Sunnyside's guests are satisfied with the hotel gyms. How Sunnyside will measure guest satisfaction, and the score that needs to be achieved before Sunnyside will extend the contract, needs to be clarified.
- Entering this management contract means having to hire an additional senior manager, as well as the support staff at each of the hotel gyms – as CFL will need to ensure that all personnel allocated to Sunnyside's hotel gyms are qualified and effective, this will increase the company's risk.
- As CFL will be required to replace the equipment in each hotel gym every two years, the company may want to consider renegotiating the initial contract term length to either four or six years. If the contract were to end in Year 5 – which is possible with the current structure of the proposal – CFL may incur higher equipment costs, given that, at the end of Year 5, the latest equipment would only be one year old.

<u>Additional information needed:</u>

- CFL needs to clarify whether the option to extend the agreement for an additional five years is determined by Sunnyside or CFL – at this point, this aspect of the agreement is unclear.
- CFL should establish what Sunnyside's expectations are relative to CFL's responsibility to keep the gym equipment well maintained. This will ensure that both companies understand the expectations from the outset of the agreement, and will reduce the chance of a dispute.

Conclusion

If CFL can mitigate or eliminate the liability risk associated with gym users becoming injured in one of Sunnyside's hotel gyms, this proposal appears strategically attractive. There is a potential synergy between this option and the Iron Depot option, and CFL's main business may benefit from the marketing that CFL would receive as a result of managing Sunnyside's hotel gyms. This proposal does not seem overly risky, and would provide a steady stream of stable and reliable income. Finally, the upfront cost of this venture is low relative to the other options. If CFL can confidently reduce the risks mentioned above, CFL should proceed with building and managing Sunnyside's hotel gyms.

Assessment Opportunity #4 (Strategic Issue #3 – Produce and stream online fitness videos using the services of Rise Edustream?)

The candidate is expected to complete both a quantitative and qualitative assessment of whether CFL should work with RiseEd to produce and stream online fitness videos.

Quantitative analysis: The candidate should assess the reasonability of RiseEd's projection and provide a revised projection and commentary on the project's potential performance. The candidate should also discuss whether the project aligns with the board's objectives to increase CFL's revenue and EBITDA.

Qualitative analysis: The candidate should discuss the advantages and disadvantages of this investment opportunity. Particular attention should be paid to the risks associated with the investment, and whether the board's objectives/preferences would be satisfied through this option.

Conclusion: The candidate should offer a conclusion that incorporates and logically follows from their quantitative and qualitative analyses.

Rise Edustream (RiseEd), a company that produces and distributes educational videos, has offered CFL its services to help CFL create fitness videos for an online platform. Under the current terms of the proposal, CFL would pay RiseEd based on the number of subscribers who sign up for the service.

Quantitative Analysis

For $2.5 million in initial start-up costs ($1.5 million for RiseEd to create the online platform, and $1 million for purchasing the videotaping equipment), CFL has the opportunity to earn revenue from the fees that subscribers to the online platform will pay in order to access the at-home workouts.

However, it is important to note that, because RiseEd provided the projection that was included in Appendix IV, there is a strong chance that these numbers are overly optimistic. This is especially likely, given the incentive that RiseEd has to make this venture appear as lucrative as possible (as, under the current agreement, the fee that goes to RiseEd will depend on the number of subscribers that the proposed online exercise platform attracts). It is also important to note that, even if the platform fails to attract even a single subscriber, under the current proposal, it appears that CFL will still be required to pay RiseEd $2 million per year for the duration of the agreement.

Therefore, an additional projection is provided that assesses the performance of the proposal at 50% of what RiseEd projected. As the projection below shows, the venture's profitability is far from certain. If CFL cannot attract at least 6,865 annual subscribers to the platform (the breakeven number of subscribers), CFL will lose money on the investment.

		Projection	
	2026	**2027**	**2028**
Number of subscribers	5,000	12,500	17,500
Subscription cost (monthly fee)	$40	$40	$40
Monthly revenue	$200,000	$500,000	$700,000
Annual revenue	$2,400,000	$6,000,000	$8,400,000
Expenses			
Fee to RiseEd	2,000,000	4,000,000	4,000,000
Labour	750,000	750,000	750,000
Marketing	500,000	250,000	250,000
General and administrative	45,000	45,000	45,000
Total expenses	3,295,000	5,045,000	5,045,000
Operating income	$(895,000)	$955,000	$3,355,000

Qualitative Analysis

Advantages:

- Exercising at home has never been more popular – this newly-proposed product would allow subscribers to do just that. Therefore, this option aligns nicely with a major trend in the industry.

- The videos would use CFL's established brand (unlike the Zenfit proposal); therefore, CFL may benefit from a significant boost to its brand awareness, depending on how many subscribers CFL can attract to the service. The effective promotion of products and services is a key success factor in the fitness industry.
- CFL would have complete control over the type of videos the company releases. The company could follow the latest trends in the industry and tailor its videos to align with these preferences.
- CFL has no experience with the technology component of this endeavor (such as creating the online platform and website, and filming, producing, and streaming the videos); however, with the proposed agreement, RiseEd would be responsible for all of those functions. This project allows CFL to enter a potentially lucrative market without having all the necessary skills provided through internal personnel.
- CFL may be able to use professional athletes to help promote, or even participate in, the fitness videos. This unique aspect of CFL's videos might help the company differentiate its product from the many competitors. However, this marketing strategy would likely be costly, and so, CFL should include these costs within the cost projection of this proposal if this is the direction the company decides on.
- There is an opportunity to develop custom equipment (with CFL's name), to compete, and to attract more subscribers. Effective innovation is a key success factor in the fitness industry.

<u>Disadvantages:</u>

- Under the current proposal, even if the new platform does not attract any new subscribers, CFL must pay RiseEd $2 million each year for the next six years. This is not reasonable. CFL needs to renegotiate the annual payment schedule because, at this point, the proposal is both unfair and very risky to CFL.
  - As part of this renegotiation, CFL should propose reducing the range between the number of subscribers that will determine RiseEd's fee. In the current agreement, RiseEd's fee will significantly increase with each additional 10,000 subscribers. To better align this fee with the number of subscribers, this range could be reduced to a gradient of each additional 2,000 or 3,000 subscribers.
- Under the current proposal, CFL would be responsible for providing subscribers with customer support. This aspect of the agreement is a significant disadvantage, given the shareholders' preference for investing in projects that are simple to operate. As CFL has no experience with providing customer support for this sort of product, it might be a big challenge to effectively provide this function. This is especially important when considering that providing good customer service is a key success factor in the fitness industry.

- As Phillip pointed out, there are many competitors within the fitness video streaming market, and that was three years ago, when CFL was researching the Zenfit contract. It is possible that CFL will not be able to attract as many subscribers as RiseEd projected.
- In order to attract an adequate number of subscribers, it seems that CFL will need to put a significant amount of time and effort toward marketing the company and the new product. This increases the complexity and uncertainty of the project, and does not align with the shareholders' preference for investing in projects that provide a reliable and stable source of revenue.
- The success of the venture also depends on the quality of the fitness instructors that CFL uses for its videos. It is unclear whether CFL has any suitable instructors for this project. Having skilled employees is a key success factor for CFL.
- CFL does not have a unique piece of equipment that the company can pair with the proposed streaming fitness videos. This may be a significant disadvantage, given that CFL's competitors have been able to secure a loyal subscriber base through doing just that.
- It is also unclear which party, whether CFL or RiseEd, will be responsible for filming the workouts. Before this option is further considered, this important aspect needs to be determined. If RiseEd requires CFL to film the workouts, this would add to the complexity of the project.

Conclusion

CFL would be taking on a significant amount of risk if the company decides to proceed with RiseEd's proposal; RiseEd is not taking on any of the risk associated with the project but will earn income no matter how many subscribers the platform attracts. Also, it is uncertain how many subscribers CFL will be able to attract to the platform, especially given the amount of competition that is already entrenched in the marketplace. Although the earning potential of the project is very high, it does not satisfy the board's objectives to reduce risk and to provide a reliable source of income. This investment is not recommended.

Assessment Opportunity #5 (Strategic Issue #4 – Open physiotherapy clinics in eight gym locations?)

The candidate is expected to complete both a quantitative and qualitative assessment of whether CFL should use the underutilized space within the eight fitness facilities to open physiotherapy clinics.

Quantitative analysis: The candidate should provide a projection of the project's performance at a varying rate of office utilization. The candidate should also discuss whether the project aligns with the board's objectives to increase CFL's revenue and EBITDA.

Qualitative analysis: The candidate should discuss the advantages and disadvantages of this investment opportunity. Particular attention should be paid to the risks associated with the investment, and whether the board's objectives/preferences would be satisfied through this option.

Conclusion: The candidate should offer a conclusion that incorporates and logically follows from their quantitative and qualitative analyses.

CFL has identified eight fitness facilities that have underutilized space, which could be used to generate additional income. This is the first of two options that CFL is considering relative to this decision.

CFL could open a physiotherapy clinic in each of the eight locations that currently have underutilized space. Each new clinic will cost $495,000 in initial renovation costs.

Quantitative Analysis

Although the revenue potential of this venture appears high, its performance is highly dependent on how many patients come to the clinics. Based on the results of a sensitivity analysis, this venture appears to be risky from a quantitative perspective. If these new clinics are not at least 60% booked each day, the venture will be unprofitable. It is unclear at this point what sort of utilization that CFL will achieve in the first few years after opening the clinics but, based on the commentary from the board meeting, it does not seem that CFL should expect 100% utilization. The uncertainty of this venture makes it riskier.

As well, given the higher relative initial investment cost, this project's payback period is less attractive in comparison with the Iron Depot and hotel gym options. From a quantitative perspective, unless CFL can reach and maintain a high utilization rate at each of its proposed physiotherapy clinics, this project will not be profitable.

Sensitivity analysis – one year of operations:

Clinic utilization	**100%**	**75%**	**50%**
Net annual revenue	$6,720,000	$5,040,000	$3,360,000
Variable costs (20% of revenue)	1,344,000	1,008,000	672,000
Staff (therapists) – fixed	2,880,000	2,880,000	2,880,000
Nav's salary	250,000	250,000	250,000
Other fixed costs	840,000	840,000	840,000
Total operating costs	5,314,000	4,978,000	4,642,000
Total operating profit	1,406,000	62,000	(1,282,000)
Add back amortization	277,200	277,200	277,200
Annual EBITDA	$1,683,200	$339,200	$(1,004,800)
Cost to build new clinics	$3,960,000	$3,960,000	$3,960,000
Payback period (years)	2.35	11.67	(3.94)

Qualitative Analysis

Advantages:

- With the increase in the popularity of exercise and fitness, more people are suffering workout-related injuries. This option takes advantage of this trend by offering healthcare services to physically injured people.
- Offering physiotherapy clinics within CFL's gyms would provide a competitive advantage because it would be offering its members this valuable service within the fitness gyms. This could help increase member satisfaction. Therefore, this option may help support CFL's core business, as offering a wide range of services is a key success factor in the fitness industry.
- CFL could hire Nav, a longtime CFL gym member, to oversee the development and operation of the new clinics. Nav appears to be qualified, as he is a highly experienced physiotherapist. His expertise in the field would likely help ensure the success of this project.
- Lenders see healthcare-related clinics in a favourable light and therefore, once CFL's new physiotherapy clinics achieve stable revenue, the company may be able to access further debt financing at favourable rates.

- Patients who are satisfied with the treatment they receive are very loyal to their physiotherapy clinics – therefore, if CFL can provide quality service to its patients, it would likely be able to build a loyal base of returning customers. This would help with the long-term viability of the project.

Disadvantages:

- The quality of CFL's potential physiotherapists would be crucial to the success of this venture. Given that CFL has no experience in this area, it may be a challenge to find and employ suitable personnel. This represents a major risk to this potential investment. If CFL proceeds, the company may want to hire a highly qualified and experienced physiotherapist to help hire the right people.
- Although Nav has offered to lead the project, CFL is unfamiliar with him and whether he is fully qualified for the position. In addition, given that Nav is a physiotherapist, he may not have a lot of experience in opening and operating a business. CFL needs more information about Nav before a hiring decision can be made.
- The success of this venture will also depend on an aggressive marketing campaign. Again, CFL's lack of experience in this sort of business may hinder the company's ability to effectively market the new clinics. It might be necessary to hire a qualified marketing agency to manage this vital aspect of the project.
- Physiotherapy is a highly specialized field, in which CFL has no experience. One of the board's objectives is to reduce risk as much as possible. This investment does not align with that objective.
- Both launching and operating these proposed physiotherapy clinics appear to be very complicated processes – this does not align with the shareholders' preference for only investing in ventures that are simple to operate.
- With this venture comes a high risk of liability – as Rosa pointed out, it will be necessary to secure a comprehensive insurance package to help reduce this risk. Nevertheless, working in the medical industry creates a whole host of new risks and considerations relative to CFL's current business model.
- Patients of the clinics would not be able to use their FRP tax credit to pay for their visits to CFL's potential physiotherapy clinics – therefore, this option does not align with a significant opportunity that has recently arisen in the health and wellness industry.
- As Rosa pointed out, the reputation of a clinic is critical to its success. Because CFL has no experience in this type of business, it might be unrealistic to assume that the physiotherapy clinics will earn a strong reputation, especially in the initial period.

- If CFL proceeds with this option, each gym in which the new clinics will be located will require parking spots to be dedicated to the clinic for accessibility reasons – the potential effect of this is unclear at this time; however, it is possible that members of these gyms will become disgruntled if their access to parking becomes more difficult as a result.

Conclusion

CFL should do more research before this option is seriously considered. The success of this venture appears highly correlated with the quality of physiotherapists that CFL can hire to staff the clinics, and the number of patients that the clinics can attract, and it is unclear whether CFL would be able to effectively manage these significant risks. Moreover, this option does not align with the shareholders' preference for reducing risk. At the moment, this option is not recommended.

It also seems unnecessarily risky to open eight new physiotherapy clinics all at the same time. If, through its research, CFL can gain confidence in its ability to attract the requisite number of patients and quality physiotherapists, perhaps it should consider opening one physiotherapy clinic at first. This will provide the company with valuable experience and information regarding whether to expand into further clinics, and is one way for CFL to reduce the risk of this investment.

Assessment Opportunity #6 (Strategic Issue #5 – Open new PurCafés in eight additional gyms?)

The candidate is expected to complete both a quantitative and qualitative assessment of whether CFL should use the underutilized space within the eight fitness facilities to open additional PurCafés.

Quantitative analysis: The candidate should calculate the incremental earnings that CFL would gain through this investment. That amount should be compared to the physiotherapy clinics.

Qualitative: The candidate should discuss the advantages and disadvantages of this investment opportunity. Particular attention should be paid to the risks associated with the investment, and whether the board's objectives/preferences would be satisfied through this option.

Conclusion: The candidate should offer a conclusion that incorporates and logically follows from their quantitative and qualitative analyses.

CFL has identified eight fitness facilities that have underutilized space, which could be used to generate additional income. This is the second of two options that CFL is considering relative to this decision.

Amanda would like to expand the number of PurCafés that are located within CFL's fitness facilities. Currently, there are five CFL locations that include a PurCafé. So far, these cafés have been successful, and Amanda would like to open a PurCafé in each of the eight fitness facilities that has underutilized space. To facilitate the expansion, Amanda also plans to lease two additional locations that will be used to process the food before it is ready for the cafés.

Quantitative Analysis

Based on the earnings report that Sandra provided in Appendix VI, the following projection was created.

PurCafés – annual earnings projection after eight new locations:

Revenues	$ 896,400
Costs	
Variable cost of food and beverages	421,300
Labour	131,000
Supplies and other costs	50,000
Amortization of fixed costs	39,000
Advertising	11,000
Total expenses	652,300
Operating profit	244,100
Number of PurCafé locations	13
	3,173,300
New lease expense	(450,000)
Net operating profit	2,723,300
Amanda's portion (20%)	(544,660)
Total operating profit to CFL	$ 2,178,640
Current operating profit (five locations)	$ 1,037,500
Incremental increase in profit	$ 1,141,140
Cost to renovate new locations	$ 2,720,000
Payback period	2.38

As a result of opening these additional PurCafés, CFL's incremental increase in operating profit would equal $1,141,140. Each new location would incur approximately $39,000 in amortization expense each year. Therefore, from this investment, CFL's EBITDA would increase by approximately $1.5 million ($1,141,140 operating profit plus $312,000 of amortization expenses).

Further, CFL can have more confidence in the accuracy of this projection relative to the physiotherapy clinic option because CFL already has experience in operating PurCafés. Therefore, the financial risk of this investment is lower than the physiotherapy option. This reduced risk will help secure CFL's current dividend, which is the shareholders' preference.

Qualitative Analysis

<u>Advantages:</u>

- Amanda's performance has been excellent to date. The current cafés are profitable and CFL's members have expressed how much they like being able to access tasty and nutritious food within their gym. CFL can expand on this success by opening more cafés.
- The demand for nutritious food has grown steadily as the popularity of healthy lifestyles has increased. By opening these eight additional PurCafés, CFL can further align itself with this industry trend.
- This option aligns well with the board's objective to invest in projects that are simple to operate. Amanda has effectively taken the lead on the first five PurCafés, and therefore, the board has not had to be very actively involved in the operation of the cafés.
- Compared to the physiotherapy clinic option, CFL is far more familiar with this option because the company already owns and operates five cafés. This decreases the risk of this investment relative to the clinics because CFL has already established the viability of including cafés within the company's fitness facilities.
- It appears that the PurCafés have benefited CFL's main source of revenue: annual membership fees. This is because the membership retention rates at the gyms that include a PurCafé have improved since the introduction of the cafés. Therefore, by accepting this option, CFL's core business may also benefit.
- CFL has also received feedback that the cafés have helped to strengthen the community atmosphere within the gym. This aligns with a key success factor within the industry. This is another indication that the PurCafés are benefiting CFL's core business.

Disadvantages:

- The success of the first five PurCafés appears to be largely as a result of Amanda's expertise and effort. Over the past few years, Amanda has opened three more of her own cafés and now wants to open eight more PurCafés. It is possible that Amanda has overextended herself and will not be able to dedicate as much time to the new PurCafés.
- In order to supply the new PurCafé locations with food, Amanda plans to lease two new food-processing locations. In addition, new staff must be hired for these locations. It might be a challenge for Amanda to ensure that the quality of food remains high. If CFL decides to accept the expanded agreement, a quality assurance stipulation should be added to it.
- Another indication that Amanda may have overextended herself are the several comments that CFL has received this year concerning the quality of the service at the cafés and the lack of availability of certain menu items. If the service quality and/or availability of menu items deteriorates further, this could affect the reputation and performance of the current PurCafés, and of any new cafés that are opened.
- The trend toward healthy lifestyles has attracted many new entrants into the market, and therefore, CFL's PurCafés will be faced with more competition from other healthy food restaurants. However, 80% of PurCafés' revenue is generated from CFL members who eat at the cafés after a workout; therefore, CFL's PurCafés may be sheltered somewhat from this new competition.
- Rosa mentioned that Amanda has been making decisions without first consulting CFL's board (such as altering menu items). If this is allowed to continue, Amanda could make decisions that do not align with CFL's mission, vision, and preferred operations. Regardless of whether the new proposal is accepted, CFL should clearly communicate with Amanda the types of decisions that the board would like to be consulted on before she implements those changes.
- With this proposal, if CFL agrees to open the additional PurCafés, Amanda's compensation will increase from 15% to 20% of PurCafés' net operating profit. As can be seen in the projection above, this would result in a very large increase to Amanda's compensation from its current level. Instead, to better ensure the effective and successful operation of the cafés, CFL may want to stipulate that a portion of those funds be put toward hiring additional personnel.

Conclusion

Given that CFL's board would like to give preference to investments that offer a secure and reliable source of revenue from an operation that is relatively easy to operate, this option appears to be superior to the physiotherapy clinics. Although the earning potential of this option is not as great as the clinics, the amount of risk that CFL would take in opening eight additional PurCafés is far lower than opening a host of physiotherapy clinics.

However, before CFL commits to this expansion, the board should meet with Amanda to discuss how she intends to operate these new locations, given her increasing workload. Although Amanda has been effective so far, it is possible that she has overextended herself and that the quality of the new and existing cafés could suffer as a result. If CFL can gain confidence in Amanda's ability to effectively expand these operations, it is recommended that CFL move forward with this option.

Summative Assessment #3 – Conclude and Advise

For Summative Assessment #3, the candidate must be assessed for reasonableness of attempt:

Yes – The candidate provided reasonable conclusions for each major issue.

Unsure – The candidate attempted to provide reasonable conclusions for each major issue.

No – The candidate clearly did not provide reasonable conclusions for each major issue.

Enabling Competencies
6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions
6.3.2 Articulates limitations to recommendations
6.3.3 Applies decision criteria to choose among viable alternatives
6.3.4 Ensures that decision criteria do not conflict with professional ethics and values

The candidate is expected to provide a logical conclusion that is consistent with their analysis and integrated with an overall recommendation of whether CFL should purchase Iron Depot, design and manage the Sunnyside Hotel gyms, produce and stream online fitness videos, and/or either open physiotherapy clinics or open new PurCafés in gyms that have available space. A competent candidate is also expected to discuss how CFL could approach financing the recommended approach.

The candidate should draw logical conclusions and make a recommendation on the strategic direction CFL should take. The candidate's analysis should integrate the analysis for all five major strategic opportunities into a coherent overall strategy. The recommendations should be strategic in nature and display good professional judgment and logic, recognizing the interconnected influence of each option. Suggesting that further information is required is acceptable where justified and consistent with the analysis.

Recommendations on Specific Issues

CFL's board would like to increase the company's revenue and EBITDA by diversifying the company into areas that offer a stable and reliable source of income. Also, because the board would like to retire from its active involvement in CFL's operations in approximately five years, it will give preference to those investments that are simple to operate. As the board members are going to rely on CFL's current $2 million annual dividend to fund their retirements, it is especially important to limit the amount of risk that the company is exposed to while making further investments. As every available investment aligns with the company's new mission and vision statements, these aspects of the situational analysis did not play a major role in the assessment of which options CFL should proceed with. As well, CFL's board should be careful to ensure that its ability to effectively manage the company's existing operations is not compromised by the time needed to ensure the success of any new investments or operations. With these considerations in mind, the following investment recommendations were made.

<u>Acquisition of Iron Depot</u>

After an adequate amount of due diligence is performed, CFL should move forward with the acquisition of Iron Depot. The business has been operational for 25 years and has seen its revenue grow steadily as the number of outlets has grown. The operation of the business also appears to be quite simple, and therefore, it is not expected that the board will need to invest a large amount of time in managing the Iron Depot outlets. Further, given the access to wholesale equipment purchases that CFL will gain through this acquisition, this investment option offers a significant synergy with CFL's core business: the fitness facilities. Of the $6.5 million that CFL currently has available for investment, this investment of $2.5 million will reduce that amount to $4 million.

<u>Contract with Sunnyside Hotel</u>

Next, it is recommended that CFL sign the management contract with Sunnyside to design and manage Sunnyside's proposed hotel gyms. Again, this option provides a fixed source of income and does not appear to be a big challenge to operate. CFL's core competency is managing fitness facilities and that is exactly what this option represents. The initial investment for this project is expected to be $650,000, which will leave CFL with $3,350,000 for any further investments.

Physiotherapy clinics or PurCafés

Finally, it is recommended that CFL choose the PurCafés option over the possibility of opening new physiotherapy clinics in the underutilized space within the eight fitness facilities. Although the earning potential of the physiotherapy clinics exceeds the PurCafés option, the PurCafés option is less risky. Therefore, the PurCafés option more appropriately aligns with the board's preference for investing in projects that offer a secure and reliable source of income. One of the main differentiating factors between these investment options is the amount of experience that CFL has in each venture. CFL has no experience in physiotherapy and would therefore need to learn an entirely new set of business practices. On the other hand, CFL is already familiar with the operation of PurCafés and can therefore be more confident in the performance of the cafés. The initial investment required to open the eight additional PurCafés is $2,720,000, and therefore, after this investment is made, the company will have $630,000 of cash remaining for further investment.

To further reduce risk, CFL may want to consider only opening two or three new PurCafés rather than eight all at once – this will help the company gain confidence that Amanda can handle the extra workload. This strategy would also provide CFL with the potential to experiment with opening one physiotherapy clinic to see whether the project is viable for a larger expansion. Again, this would help CFL contain the risk of these ventures, which aligns with the preferences of the board members.

Produce online fitness videos

It is not recommended that CFL proceed with the agreement with RiseEd to produce streaming fitness videos. Not only is the current agreement with RiseEd unfair but CFL's ability to attract and retain an adequate number of subscribers to the new fitness streaming platform is far from certain. The costs associated with this investment are simply too high. Based on the board's stated objectives and preferences, this option is not suitable.

Here is a summary of the recommendations and the affect each would have on the company's available funds for new investment projects:

Current available investment capital	$6,500,000
AO2 Iron Depot acquisition	-$2,500,000
AO3 Sunnyside contract	-$650,000
AO4 Streaming fitness classes	*Do not proceed*
AO5 Physiotherapy clinics	*Do not proceed*
AO6 New PurCafés	-$2,720,000
Total cash remaining	**$630,000**

Summative Assessment #4 – Communication

For Summative Assessment #4, the candidate must be assessed for reasonableness of attempt:

Yes – The candidate adequately communicated their response.

No – The candidate clearly did not adequately communicate their response.

Insufficient communication in a candidate's response would generally include some of the following:

- The reader needs to re-read sections several times in order to gain an understanding.
- It is not clear what point the candidate is trying to make.
- The quantitative analysis does not make sense because of a lack of labelling or illogical ordering.
- There is an excessive amount of spelling and grammatical errors.
- Unprofessional language is used.

Summative Assessment #5 – Overall Assessment

For Summative Assessment #5, the candidate must be assessed in one of the following, based on their overall performance:

Clear Pass – Overall, the candidate provided an adequate response, clearly meeting the minimum standards for each of the summative assessments above.

Marginal Pass – Overall, the candidate provided an adequate response, with some errors or areas of omission, but the underlying key concepts were there.

Marginal Fail – Overall, the candidate provided an attempt at a response, one that contained several errors or where the analysis was incomplete.

Clear Fail – Overall, the candidate did not provide an adequate response; the response was deficient in multiple areas.

To be assessed a Pass, the candidate is expected to perform adequately in all the summative assessments and demonstrate that, overall, they addressed the issues of all of the shareholders.

In making their overall assessment, markers were asked to consider the following:

1. Did the candidate step back and see the bigger picture, and then address the broader issues identified?
2. Did the candidate prioritize the issues by discussing the major and minor issues in appropriate depth?
3. Did the candidate use both quantitative and qualitative information to support their discussions and conclusions?
4. Did the candidate use the appropriate tools to perform quantitative analysis?
5. Did the candidate use sufficient case facts (current case and Capstone 1 case) about the external and internal environment to support their discussions?
6. Did the candidate communicate their ideas clearly, integrating and synthesizing the information?

SAMPLE RESPONSE – CFL VERSION 2

Below is an actual passing candidate response.

To: Board of Directors, CanDo Fitness Ltd. (CFL)
From: CPA, Serringers Consulting Group (SCG)Date: May 1, 2025
RE: Situational Analysis and Analysis of Strategic Options

In this memo, I have performed a current situational analysis for CFL and utilised my understanding to analyse each of the future strategic option brought forth by the board.

<u>Part I: Current Situational Analysis</u>

<u>Vision</u>:

To provide equipment, classes, and other amenities and services in a friendly and welcoming atmosphere to motivate and help individuals to achieve a healthy lifestyle.

The vision statement was updated in late 2022 to reflect the addition of additional offerings such as the PurCafes and the climbing facilities.

<u>Mission</u>:

To provide the means for people of all ages to embrace a fit and healthy lifestyle, providing state-of-the-art equipment and innovative, fun and challenging group classes.

The mission statement was updated in late 2022 to better reflect the board's desire to cater to people of all ages. The focus on local communities was also removed from the mission statement.

<u>Values</u>: The corporate values remain unchanged.

- All employees are caring and understanding of members and work as part of a team.
- Continuously update equipment to ensure that it is leading edge and provide ever-changing group classes to stay up to date with current trends.
- All staff are committed to their own fitness goals and healthy living.
- Strive to build a community of friends in a safe and supportive environment and be a driving and vocal force in the local community.

- Provide activities that are fun, challenging and designed to help individuals achieve their fitness goals.

Objectives

The board is looking to make further investments to further diversify CFL's sources of revenues. The objective for investments made is to increase both revenues and EBITDA. The board, however, has a preference for less risky projects that are simple to operate and provide a stable and reliable source of revenues in order to protect the company's dividends.

Financial Analysis

Revenues: Overall, additional revenues have been generated and are attributed to the addition of the climbing walls and PurCafes. In terms of PurCafe revenues, 80% of these revenues are generated from CFL members who eat in the cafe after a workout and the other 20% is from non-members who only come to the gym to use their cafe.

Liquidity: CFL currently has $6.5 million available for new investment projects.

Solvency: CFL has no more room to raise additional debt.

Overall Financial Situation: Overall, CFL's financial situation has improved since 2022 through increase in revenues as a result of increased member retention.

Industry Key Success Factors:

- Easy Access to Members
- Clean Facilities
- Member retention
- Have multiple locations
- Offer Wide Range of services
- Effectively promote products and services
- Being innovative to meet ever-changing demands for members

SWOT Analysis

Strengths

- Both the indoor wall and PurCafe investments pursued in 2022 have been successful, which creates a diversified source of revenue for CFL.

- CFL successfully negotiated an agreement with fitness instructors and began paying them for all hours worked, which has led to improved the quality of fitness classes. A better quality of classes increases member retention for CFL, making revenues more stable.

- Amanda is determined and would like to further expand the PurCafe offering, which means that Amanda is clearly committed to continued operation of PurCafe. This means continued revenues from this source for CFL.

- Members have provided positive feedback for the first five PurCafe locations and love having easy access to tasty nutritious food. This means CFL is current meeting the key success factor of easy access for clients and is keeping high customer satisfaction at these locations.

Weakness:

- CFL is constrained in its ability to raise additional debt financing, which can limit the strategic options that CFL can undertake.

- The board is discussing reducing their involvement in the day-to-day operations of CFL, which means that an improper succession planning for this change in their roles can lead to operational inefficiencies and ultimately impact member experience.

- There are currently eight CFL fitness facilities with underutilised space, which means that CFL is currently missing out on potential revenues and still having to fund operating costs for that space.

- Amanda has been making decisions on her own lately and made changes to the menu without discussing with the board, which may mean a lack of communication between the two parties in the arrangement and lead to inefficient operations.

Opportunity:

- In recent years, the popularity of healthy lifestyle choices has growth considerably, resulting in a higher demand for fitness products and services. This provides CFL with an opportunity to capitalise on the trend by offering more products and attracting additional members.

- The demand for nutritious food options has grown steadily, which increases the growth opportunity for CFL's PurCafe offering.

- The government of Canada unveiled a new Fitness Rebate Program (FRP) to provide tax credits for Canadians who purchase products and services related to exercising, which means members may be more likely to get membership at gyms like CFL or spend in additional offerings such as the climbing walls.

- Due to the increase in demand for fitness, there are also increases in exercise-related injuries, which provides CFL with an opportunity to offer a physiotherapy service and further diversify revenue streams.

Threats:

- Despite growing overall popularity of fitness, the convenience of working out at home as also become popular, which threatens brick and mortar gym like CFL's ability to maintain membership levels.

- Trend towards healthy lifestyle has attracted many new entrants to the market, which threatens CFL's market share and revenues.

Key Constraints:

- Must spend $4 million annually on new gym equipment to ensure its fitness facilities stay up to date

- CFL has $6.5 million available for new investment projects but no access to further debt financing

Key Risks: The key risk that CFL faces is the growing popularity of at-home workouts as customers want more convenience. Moreover, the entry of new members in the industry is also a threat for CFL.

Conclusion:

CFL's investment in the indoor climbing walls and PurCafe have led to an improvement in the company overall financial situation. Moreover, improvement in fitness instructor relationship have led to better quality classes and thus increased member retention. In order to fund the investments, however, CFL incurred additional debt and now faces a constraint on its ability to obtain additional funding through debt. With these factors in mind, I will use the following factors to assess each of the strategic options considered by the board:

- Impact on Revenue

- Impact on EBITDA

- Alignment with Overall Strategic Direction

Part II: Analysis of Major Issues

Iron Depot

The board is considering a potential purchase of Iron Depot.

Quantitative Analysis

Please see Exhibit A of the excel for calculations.

In order to asses this option quantitatively, I performed an EBITDA-based valuation to assess a fair value for Iron Depot.

Based on the calculation performed, Iron Depot is worth $10.2 million, which is more than the asking price of $10 million. This means that the asking price is fair. The purchase of Iron Depot should positively impact CFL's revenues as well as EBITDA given the 2024 numbers.

Quantitative considerations:

- We are unaware of whether and how much depreciation and amortization is based on the statements provided by Frank. These figures can impact the true valuation number.
- The valuation also assumes that the manager and staff members will stay with the company at the same wages, however this may not be true as staff could want to exit the company following a new takeover.

Overall, quantitatively this option is sound as the asking price is below the fair value and it is reasonably expected to increase both revenues and EBITDA, which meet the board's objective with new investments.

Qualitative Analysis: We will perform a pros and cons analysis to assess this option qualitatively.

Pros of Purchasing Iron Depot

- Purchasing Iron Depot means that CFL will receive at least a 20% discount on future equipment purchases, which allows CFL to further increase EBITDA and meet the board's objective for future investments.
- The board's objective is to diversify revenues. Entering into this new equipment sales industry allows CFL to achieve this objective.
- The current owner of Iron Depot is willing to provide a $7.5 million loan to the purchaser, which means that CFL will only incur $2.5 million in upfront cash. This aligns with CFL's current constraint of only having $6.5 million to invest in future options.
- A current industry trend is the growth of at-home fitness as customers want convenience. Purchasing Iron Depot allows CFL to capitalise on the growth of this trend.

Cons of Purchasing Iron Depot:

- The current owner plans to retire completely after the sale, which could impact operations as well as Iron Depot's level of customer service, which is a key success factor.

- The company's main contributor to success are three supplier contracts, which may indicate that if these suppliers decide to end their contracts earlier than the 10 years, Iron Depot's revenues could be significantly impacted.

- Most of Iron Depot's customers are fitness facilities, which means that if CFL purchases Iron Depot, they may take their business elsewhere in an attempt to not benefit a competitor. This will impact Iron Depot's performance and CFL's ROI.

Recommendation:

Based on the analysis performed, Iron Depot's asking price is fair as the valuation I performed showed a value of $10.2 million. Qualitatively, this option allows CFL to diversify its revenues and increase its EBITDA through both Iron Depot's continued operation as well as the incremental savings on equipment purchase. Moreover, it is also mentioned that Iron Depot's business model is quite basic, which aligns well with the board's objective for investment options to be low risk. This option is also plausible financially as the upfront cash outflow is $2.5 million. As such, I recommend that CFL proceed with the purchase of Iron Depot.

<u>Sunnyside Hotels</u>

Sunnyside has approached CFL and asked if CFL would be interested in managing gyms at seven of their locations.

<u>Quantitative Analysis:</u>

Please see Exhibit B for the calculations performed.

I performed an NPV Analysis for this contract with Sunnyside to assess whether the contract is profitable for CFL. Per the calculation performed, this project has an estimated NPV of $1,055,265. This calculation is based on a discount rate of 12% and an assumed tax rate of 26%.

An additional assumption behind the NPV calculation is that the wages for the staff and the senior manager will remain constant until 2030, which may not be the case due to inflation. Moreover, I have also assumed that the cost of the equipment replacement will remain constant, which may not be case if costs rise.

Overall, this option's positive NPV suggests that it will positively impact CFL's EBITDA. Since Incremental revenues exceed costs, the board's objective of growing revenues is also met. CFL will be able to finance the initial costs as well as the ongoing costs with this option as initially only $650,000 is required and subsequently the inflows from Sunnyside can cover the costs. As such, quantitatively this is a sound option.

Qualitative Analysis:

I have performed a pros and cons analysis for this option below.

Pros of entering into the SunnySide Contract:

- CFL's mission is to provide means for people of all ages to embrace a fit and healthy lifestyle, which means that addition of new gyms in these hotels is in alignment with its mission.

- One of the objectives for the board is for projects to provide stable and reliable source of revenue. Given that this agreement would lead to fixed payments from Sunnyside to CFL, this objective is met.

- A key industry success factor is having multiple locations, which means that opening seven new locations can lead to CFL attracting more members that are closer to these hotel locations.

Cons of entering into the SunnySide contract:

- One of the board's objectives is to diversify its source of revenues. Opening new gym locations means CFL stays within the same business model and does not lead to revenue diversification.

- The gym spaces will have limited space, which means that the overall quality of the gym may not be up to par with other CFL locations. This can negatively impact customer service, which is a key success factor.

- The cost of equipment or expected frequency of replacement may be faster than every two years, both of which significantly impacts the profitability of the project.

- Since CFL does not have experience operating within a hotel space, there may be additional risks such as theft of equipment by travelling guests that impact the profitability of this project.

Recommendation:

Based on the analysis performed, this project is profitable as it generates a NPV of $1,055,265 and helps increase both revenues and EBITDA. Qualitatively, a major advantage of the project is the stability of future revenues, which aligns with the board's objective. This option also allows CFL to increase its number of locations. These pros outweigh the cons of lack of diversity in revenue and potential unforeseen costs from lack of experience in a hotel setting. As such, I recommend that CFL enter this agreement with SunnySide.

<u>Rise Edustream (RiseEd)</u>

RiseEd has offered CFL the opportunity to use their services in order to create fitness videos for online platforms.

<u>Quantitative Analysis</u>

See Exhibit C for the calculations.

While the forecast provided shows a positive operating income for all three years of the forecast, the growth forecast is aggressive as members are assumed to increase 250% in 3 years.

As such, I assessed the sensitivity of this projection by changing the growth rate of subscribers to a moderate 20% growth per year, which showed that the operating income in 2028 became negative. This makes sense as the project's expense structure is comprised primarily of fixed costs and the fee to RiseEd is on a step-fixed cost basis.

Some other considerations:

1. The labour and marketing costs are assumed to be fixed, which may not be reasonable if costs rise in the future due to inflation. This will negatively impact the profitability of the project.

Quantitative Assessment: Based on the calculation performed, I find that the projection for the streaming classes is aggressive and depend on several factors such as the fixed labour costs as well as effectiveness of CFL's marketing. If the growth rate is changed to a moderate growth of 20% per year, the operating income in 2028 becomes negative and the sum of annual operating income under this assumptions are below the initial, providing a negative NPV. As such, quantitatively this project is not appealing as there are several uncertainties and a potential negative impact to EBITDA if growth rate is 20% or below.

Qualitative Analysis

Pros of Partnering with RiseEd

- Innovating to meet ever-changing demands of customers is a key success factor in the industry and engaging in the fitness video production allows CFL to meet this success factor and attract new members

- Since CFL is in complete creative control regarding the type of videos released, CFL can product videos in yoga, cardio, meditation. This aligns with CFL's value of providing activities that are fun.

- Releasing fitness videos that subscribers can use at home allows CFL to capitalise on the trend of customers choosing products and service that provide convenience of workout out at home.

- This option allows CFL to brand the videos under the CFL brand, which increases CFL's brand exposure and could lead to new members wanting to try other CFL offerings.

Cons of Partnering with RiseEd

- As new entrants continue to enter the industry and other competitors also provide videos, there is high competition in the fitness video space that could impact the success of the project.

- The board's objective and preference is for projects that are less risky. Since CFL is charged $2 million annually for 10,000 subscribers or part thereof, there is a financial risk of incurring the fixed fee regardless despite growth in subscribers, making this option risky.

- By offering fitness videos, CFL may also be cannibalising its own members who would rather enjoy the videos from CFL instructors at their own homes. This is against the key success factor of member retention.

Recommendation:

Per my analysis, this project's financial projection is uncertain and a change in the growth estimates to 20% showed that the project would become unprofitable. This means that the project is risky and depends on several factors such as CFL's marketing, which is against the board's preference for less risky investments. Moreover, the video streaming industry is highly competitive and makes this option more risky. As such, I do not recommend this option for CFL.

Underutilised Space

CFL has 8 facilities with underutilised space and the board is considering between:

i) Offering Physiotherapy services

ii) Opening additional PurCafe Locations

Option 1 - Opening physiotherapy services

Quantitative Assessment

Please see Exhibit D for calculations.

Based on the calculation performed, this option provides positive incremental EBITDA of 339,200 under 75% utilisation and $1,683,200 under 100% utilisation. This means that under these scenarios, this project meets the board's objective of increasing revenues and EBITDA.

Option 2 - Opening new Purcafe locations

Quantitative Assessment

Per my calculation in Exhibit E of the attached excel, this expansion should generate an annual incremental EBITDA of $1,514,240. This is based on the assumption that the new locations will have a similar revenue and cost structure as the current 5 locations.

Quantitative Conclusion: Comparing the two options quantitatively, it is evident that the Physiotherapy option provides the highest incremental EBITDA of $1,683,000 under the 100% utilisation scenario. However, this is uncertain and going to the 75% scenario reveals a lower EBITDA of $339,200. The annual incremental EBITDA of the PurCafe option is $1,514,240 and this projection is more stable as CFL already has performance history of the previous 5 PurCafe locations. Thus, quantitatively, the physiotherapy option at 100% utilization is the best option. However, qualitative factors must be considered.

Qualitative Analysis: I have completed a pros and cons analysis for the two options.

Pros of Pursuing the physiotherapy option (Con of Pursuing the PurCafe Expansion)

- Pursuing the physiotherapy option allows CFL to capitalise on the growing trend for the demand of physiotherapy services and attract additional members looking for these services.

- One of the key success factors in the industry is offering a wide range of products and services and CFL will be able to meet this key success factor by introducing the physiotherapy service, which is a new offering for the facilities. Conversely, expanding the PurCafe location would not meet this KSF.

- Offering the physiotherapy services is also aligned with the board's objective of diversify CFL's sources of revenues. This would not be met if the PurCafe expansion was pursued.

- One of the threats identified in the situational analysis was that there are far more restaurants and cafes that offer healthy choices. This means that this space could be getting increasingly competitive and that the current success of Purcafe locations may not continue.

Pros of Pursuing the PurCafe option (Con of Pursuing the Physiotherapy Option)

- In the situational analysis, I identified a growing trend in the industry where customer demand for nutritious food has growth steadily. Pursuing the PurCafe expansion would allow CFL to capitalise on this opportunity and increase revenues.

- One of PurCafe's strengths is the positive feedback that members provided for the PurCafe location. Opening additional PurCafe locations would therefore allow CFL to continue growing this strength and increasing customer satisfaction.

- Amanda has continued to be determined in operating PurCafe locations and has created value for CFL by handling the logistical side of operations, which means that this expansion will allow the board to continue being more-hands off and focus on other operations of CFL.

- Member retention rates at the five locations increased, which is a key sucess factor for the industry and opening new locations in the 8 CFL gyms could help member retention there as well.

Recommendation:

Based on the factors considered, I recommend that CFL pursue the PurCafe expansion because the incremental EBITDA of $1.514 from this option is subject to less uncertainty than the various scenarios possible for the physiotherapy option. This aligns better with management's preference for a less risky investment while also allowing CFL to increase revenues and EBITDA. Qualitatively, PurCafe has received positive customer feedback and helped reduce retention at its locations, which is a key success factor.

Operational Issues

Succession Planning

Issue: The board has indicated the desire to reduce day to day involvement in CFL's operations within the next 5 years and hand the company's management function to CFL's management.

Implication: With the entire management aiming to reduce involvement and hand over responsibilities, it is important that the board is considering succession planning steps. Given that the five board members have been with the company for a long duration, effective succession planning will be important in order for CFL to continue operating effectively and providing good customer service, which is a key success factor.

Recommendation: Over the next five years, I recommend that the board identify senior managers who the board deems more capable of replacing their roles. Each management role, such as HR and marketing must be considered and the ideal person with the right skill-set for that particular role should be scouted. Then, the board should train the prospective senior managers over a period of two years to ensure they are effective when promoted.

Amanda's Workload

Issue: Amanda appears to be spread too thin as she has taken on multiple responsibilities.

Implication: Since Amanda has opened three of her own vegetarian restaurants on top of the 5 PurCafe locations she operates, there have been signs of potential impact on quality of PurCafe. Some customers indicated that the quality of service at the cafes declined and other mentioned that certain items were unavailable. This impacts CFL's customer service, which is a key success factor and also directly impacts revenues as less customers may want to return to PurCafe.

Recommendation: I recommend that the board have a discussion with Amanda regarding her workload as well as provide her constructive feedback based on what customers have said. The board should suggest that Amanda should commit to managing only the PurCafe locations and getting a manager for her vegetarian restaurants if she wants to take on the 8 more additional locations.

Overall Recommendation:

CFL's current situational analysis shows that the company has had success through its investment in the climbing walls and PurCafe. The board's objective for future investments is to increase revenues and EBITDA while avoiding taking on risky projects. Accordingly, I analysed each strategic option presented and provide the following recommendations:

- CFL should proceed with the investment in Iron Depot as the asking price is below its calculated fair value, making the option financially sound. Moreover, this investment option provides an opportunity to diversify revenues while investing in a simple business model, which aligns with the board's objective.

- CFL should proceed with the Sunnyside Hotel Gym Management Contract as this option allows CFL to generate stable annual revenues and EBITDA while expanding its locations.

- CFL should not proceed with the streaming fitness video agreement with RiseEd as the forecasts provided by RiseEd having many uncertainties. A sensitivity analysis by changing the growth forecast to 25% per year resulted in the investment becoming unprofitable, which is against the board's objective of increase EBITDA. Moreover, the video streaming industry is highly competitive and makes this option more risky.

- CFL should work with Amanda to open the 8 new PurCafe locations in the underutilised gyms as this option allows CFL to increase its annual revenues and EBITDA while also capitalising on the trend of growing demand for nutritious food. When operated effectively, the PurCafe locations have also shown an ability to increase member retention.

    - As discussed in the operating issue, the board should ensure that you obtain a commitment from Amanda that she will focus on managing the PurCafe locations only and get a manager for her vegetarian restaurants. This will ensure that Amanda's workload is not split between two restaurants and allow PurCafe to improve on the feedback received from customers.

- The board should ensure that a succession planning is put in place and capable senior managers are selected and trained over the next 5 years to avoid operational issues when the board hands off the management responsibility.

Since financing is a key constraint for CFL, I have ensured that the options recommended are within the $6.5 million available for new projects. The total upfront investment required for the three strategic options is $5,870,000 ($2.5M for Iron Depot, 650k for Sunnyside Hotel, and $2.72M for PurCafe).

Each of the strategic options recommended also align with the overall strategic direction for CFL whereby the board wants to diversify revenues and EBITDA through investing in preferably less risky and stable investments.

The next steps for the board are as follows:

1. Inform Iron Depot the intent to purchase the company and finalise purchase terms after performing additional due diligence, particularly on the physical condition of the stores.

2. Inform SunnySide the intent to proceed with the contract and begin scouting for an effective senior manager who can oversee the gym operations.

3. Sit down with Amanda to discuss next steps for the 8 new locations and also discuss her overall workload improvement, as recommended in my operational issue analysis.

Exhibit A: Analysis of Iron Depot
Purpose: To perform a Valuation for Iron Depot

Operating Income	$ 2,167,800.00	
Normalizing Adjustments		
One-time expense	$ 450,000.00	
Add-back: Owner's salary	$ 75,000.00	
Less: Market rate salary	$ (115,000.00)	
Adjusted Operating Income	$ 2,577,800.00	
Multiple	$ 4.50	Given
Valuation	$ 11,600,100.00	
Less: Debt	$ (1,400,000.00)	
Add: Cash	$ 10,000.00	
Net Valuation	**$ 10,210,100.00**	

Conclusion: Based on the valuation performed, Iron Depot is worth $10.2 million, which means the asking price of $10 million is fair.

Exhibit B: Sunnyside Hotels
Purpose: To assess the quantitative impact of opening new gyms at Sunnyside

	Upfront	**2026**	**2027**	**2028**	**2029**	**2030**
Incremental Revenues		$ 1,850,000.00	$ 1,850,000.00	$ 1,850,000.00	$ 1,850,000.00	$ 1,850,000.00
Incremental Costs						
Staff Member		$ 817,600.00	$ 817,600.00	$ 817,600.00	$ 817,600.00	$ 817,600.00
New Senior Manager		$ 115,000.00	$ 115,000.00	$ 115,000.00	$ 115,000.00	$ 115,000.00
New Equipment (every two years)				$ 650,000.00		$ 650,000.00
Annual Cash Flow		$ 917,400.00	$ 917,400.00	$ 267,400.00	$ 917,400.00	$ 267,400.00
Tax (26%)		$ 238,524.00	$ 238,524.00	$ 69,524.00	$ 238,524.00	$ 69,524.00
After-tax Cash Flow	$ (650,000.00)	$ 678,876.00	$ 678,876.00	$ 197,876.00	$ 678,876.00	$ 197,876.00
NPV	**$ 1,055,265.56**					

Note A: Calculating Staff Wage		
Number of days per year	365	
Open Hours	16	*6 AM to 10 PM*
Total Hour per location	5840	
For 7 locations	40880	
Hourly wage	20	
Total Annual Wage	817600	

Conclusion: Based on the calculation performed, the NPV of this contract is $1,055,265. This means that the project is quantitatively sound, however, qualitative factors must be considered.

Exhibit C: Streatming Fitness Classes
Purpose: To assess quantiative impact of partnering with RiseEd

Projected	Upfront	2026	2027	2028	
Projected Income		$ 1,505,000.00	$ 4,955,000.00	$ 7,755,000.00	Given
Tax (Assuming 26%)		$ 391,300.00	$ 1,288,300.00	$ 2,016,300.00	
After-tax Cash Flows	$ (2,500,000.00)	$ 1,113,700.00	$ 3,666,700.00	$ 5,738,700.00	

Sensitivity - If Subsribers Increase moderately 20%per year)	Upfront	2026	2027	2028	
Number of Subscribers		10,000.00	12,000.00	14,400.00	
Monthly Fee		40	40	40	
Annual Revenue		$ 4,800,000.00	$ 5,760,000.00	$ 6,912,000.00	
Labour		$ 750,000.00	$ 750,000.00	$ 750,000.00	Fixed
Marketing		$ 500,000.00	$ 250,000.00	$ 250,000.00	Fixed
General and administrative		$ 45,000.00	$ 45,000.00	$ 45,000.00	Fixed
Fee To RiseEd		$ 2,000,000.00	$ 4,000,000.00	$ 6,000,000.00	
Total Expenses		$ 3,295,000.00	$ 5,045,000.00	$ 7,045,000.00	
Operating Income		**$ 1,505,000.00**	**$ 715,000.00**	**$ (133,000.00)**	

Conclusion: While the forecast provided shows a positive operating income from the proejct, the growth estimates appear aggresive. I performed a sensitivy analysis and assumed a moderate growth of 20% in subsribers per year, which revelaed that the project could become unprofitable in 2028.

Exhibit D: Physiotherapy Clinics
Purpose: To assess financial impact of opening physiotherapy clinics

	50% utilization	75% utilization	100% utilization	
Incremental Revenues	$ 3,360,000.00	$ 5,040,000.00	$ 6,720,000.00	
Variable Costs	$ 672,000.00	$ 1,008,000.00	$ 1,344,000.00	*20% of revenues*
Physiotherapist Salary	$ 2,880,000.00	$ 2,880,000.00	$ 2,880,000.00	*4 physiotherapists each for 8 locations*
Fixed Costs	$ 840,000.00	$ 840,000.00	$ 840,000.00	*105k per clinic*
Nav Salary	$ 250,000.00	$ 250,000.00	$ 250,000.00	
Earnings	$ (1,282,000.00)	$ 62,000.00	$ 1,406,000.00	Note A
Add back: Depreciation	$ 277,200.00	$ 277,200.00	$ 277,200.00	
Annual EBITDA	-1004800	$ 339,200.00	$ 1,683,200.00	
Upfront Investment	$ 3,960,000.00	$ 3,960,000.00	$ 3,960,000.00	495k for 8 locations
payback period	N/A	11.67	2.35	

Note A: Annual Depreciation		
Per clininc cost	346500	70% of initial cost
Total Equipment	2772000	
Annual Depreciation	277200	*Given 10 year useful life*

Conclusion: The physiotherapy Clinincs provide positive Incremental EBITDA under the 75% and 100% utilization scenarios.

Exhibit E: Purcafe Expansion

Purpose: To asess the incremental EBITDA from the 8 new PurCafe locations.

Initial Costs	$ 2,720,000.00	340k per location
Operating Profit for 8 locations	$ 1,952,800.00	*244,100 per average location for 8 locations*
Less: Incremental Cost		
Lease Expense	$ 450,000.00	*225k each*
Incremental Operating Income	$ 1,502,800.00	
Amanda's portion	$ 300,560.00	*20% for Amanda*
Incremental Operating Income for CFL	$ 1,202,240.00	
Add: Amortization for all locations	312000	39k per location
Incremental EBITDA	$ 1,514,240.00	

Conclusion: The additional purCafe locations will generate an incremental EBITDA of $1,514,240.

APPENDIX G

RESULTS BY SUMMATIVE ASSESSMENT OPPORTUNITY FOR DAY 1 VERSION 1 AND VERSION 2

Results by Summative Assessment Opportunity

Marking Results – CanDo Fitness Ltd. Version 1

Indicator	Papers	Did not meet standard[1]	Marginal[1]	Yes, met standard
Situational Analysis	5425	0.07	1.05	98.88
Analysis	5425	2.12	19.78	78.10
Conclude and Advise	5425	3.08	22.49	74.43
Communication	5425	0.00	0.18	99.82

Marking Results – CanDo Fitness Ltd. Version 2

Indicator	Papers	Did not meet standard[1]	Marginal[1]	Yes, met standard
Situational Analysis	663	0.90	9.65	89.44
Analysis	663	3.47	40.87	55.66
Conclude and Advise	663	2.11	55.05	42.84
Communication	663	0.00	0.45	99.55

[1]Clearly failing papers (i.e., did not meet the standard) were marked twice. All marginally failing or marginally passing papers were marked a second time to determine which ones met the passing standard. A selection of papers that were close to the margin were also looked at by third marker. The clear pass papers were marked only once, however, they were audited.

The BOE ensures that Version 2 difficulties are equated with Version 1. Any differences in the above statistics are attributable to the mix of candidates writing, which varies with each version.

APPENDIX H

BOARD OF EXAMINERS' COMMENTS ON DAY 1 SIMULATIONS
VERSION 1 AND VERSION 2

BOARD OF EXAMINERS' COMMENTS ON DAY 1
(CFL VERSION 1)

Paper/Simulation:	Day 1 – Linked Simulation CFL V1 (on September 2022 CFE)
Estimated time to complete:	240 minutes
Simulation difficulty:	Average
Competency Map coverage:	N/A; Enabling Skills

Examiners' comments by Summative Assessment Opportunity (SO)

SO#1 (Situational Analysis)

Candidates were expected to highlight the factors, both internal and external to CFL, that would have an influence on the strategic decisions presented in the simulation. Since Capstone 1, candidates were informed that the number of members at CFL's traditional fitness gyms had continually declined and that, without a significant shift in strategic focus, these gyms were unlikely to survive. Also since Capstone 1, CFL entered into an agreement with Zenfit to become the Western Canadian distributor of Zenfit products and to livestream videos for Zenfit's online exercise platform, and converted eight of its fitness gyms into climbing facilities. In addition, in late 2024, Rosa decided to resign from CFL's board, and wanted to sell her common shares of CFL as soon as possible.

Within the Day 1 simulation, candidates were informed that CFL's board wanted advice on which age demographic to target in order to improve the performance of the company's fitness gyms. CFL's board had the further objective of improving the company's EBITDA in the coming years. With these objectives in mind, candidates were expected to analyze the various strategic options that were presented in the simulation. Internally, CFL had only $2 million of cash available for strategic investment, a limitation that was made worse by the fact that CFL did not have access to any further debt, given the reluctance of lenders to extend credit to smaller fitness companies (defined as fitness companies that had fewer than 50 locations). Despite these cash limitations, CFL also had the opportunity to sell two of its business units: the Zenfit distribution/video production agreement, and the company's climbing wall facilities. Candidates were rewarded when they made relevant links between their situational analysis and their analysis in SO#2, and recommendations in SO#3.

Most candidates provided a sufficient discussion of CFL's situation at the beginning of their response. Most candidates provided an updated SWOT analysis that highlighted the changes in the company's situation that had occurred since Capstone, and identified the board's main objectives to be considered in relation to the strategic options that were presented in the simulation. Most candidates recognized the limited investment capital that CFL had available, and the fact that CFL was unlikely to obtain further investment capital through adding more debt. Most candidates also recognized that the industry had become highly competitive, which was the likely reason for the deteriorating performance of CFL's fitness gyms; however, despite recognizing this, many candidates did not incorporate this aspect of the situational analysis into their discussions of the strategic options that were available.

Strong candidates provided a situational analysis that both identified and discussed the implications of the situational aspects presented in the simulation, with a better focus on the major considerations, such as the risk associated with CFL's rapidly dropping membership numbers at the company's fitness gyms. Strong candidates often incorporated the fact that the industry had become highly competitive in their discussion of the strategic options (for example, they routinely recognized the risk that Zenfit's product sales may continue to drop, given the release of many new, technologically advanced fitness machines by CFL's competitors). Strong candidates did a good job of recognizing that CFL's objective of targeting a specific age demographic would impact the viability of the other strategic decisions that were to be made, and linked their discussions of these decisions to the preferences of each age demographic (for example, within AO6, strong candidates recognized Albert's expertise as a yoga teacher, and how that would be an advantage, given the older demographics' preference for that activity). Strong candidates also discussed CFL's limited investment capital in greater depth, and linked this constraint to their discussion of each investment option.

Weak candidates tended to simply list information from Capstone 1 related to key success factors, mission, and vision, without identifying or discussing which of those items would have the most influence on their decision-making process. Weak candidates also tended to make more generic links back to their situational analysis while analyzing each of the strategic options presented in the simulation (for example, many weak candidates repeatedly discussed whether each option aligned with CFL's mission and vision, despite the fact that all of the options presented in the simulation aligned well with CFL's mission and vision statements). Weak candidates also tended to highlight CFL's cash position as a strength even though most of the options available to CFL required more than the cash available (for example, to target the under-40 age demographic, CFL would need to invest $7 million annually in new equipment, to satisfy their type of equipment preference).

SO#2 (Analysis of the Issues)

Candidates were expected to analyze four strategic options, both qualitatively and quantitatively. Candidates were also expected to discuss whether either Louisa Rice or Albert Fong would be an appropriate replacement for Rosa on CFL's board.

AO#2: Which age demographic should CFL target for its fitness gyms?

Given the deterioration of the membership numbers at CFL's fitness gyms, candidates were directed to analyze and recommend which age demographic, either under-40 or over-55, CFL should target in order to improve the performance of these gyms. Qualitatively, candidates were expected to discuss the advantages and disadvantages of each age demographic while also recognizing the main situational aspects that would impact the decision (such as the increase in competition, particularly for gyms that were equipped with modern, high-tech equipment). Candidates could have recognized the apparent tradeoffs between the age demographics (for example, although CFL currently had more members from the under-40 group, the over-55 demographic seemed more likely to remain as members, given their connection to the gym's community). Quantitatively, candidates were expected to provide an earnings projection for each demographic, and then discuss which option would more likely improve CFL's EDITBA, which is one of the board's main objectives.

Most candidates identified and discussed enough qualitative considerations in relation to this strategic decision. Most candidates recognized that more of CFL's current members were from the under-40 demographic, and that the growth of this group was greater than the over-55 demographic. Most candidates also discussed how the older demographic was willing to pay more for their gym membership if the gym suited their preferences. Quantitatively, most candidates attempted to project the earnings that CFL could expect if the company were to target either the under-40 or over-55 age demographic. This was most often accomplished by providing a three-year EDITBA projection. A common mistake that many candidates made was to include the annual equipment investment costs as an operating expense within their EBITDA calculations. Another common mistake was failing to recognize that the annual cost of adequately equipping the gyms to suit each demographic ($7 million for the under-40 demographic and only $1 million for the older demographic) would have impacted the viability of each option.

Qualitatively, strong candidates highlighted the seeming disparity of industry competition that existed between the two demographics. These candidates correctly pointed out that most of the new competition within the industry was focused on modern facilities that were equipped with high-tech equipment, a trend that opposed the preferences of the over-55 demographic. Strong candidates also highlighted that the equipment preferences of the over-55 demographic did not align with CFL's current mission and key success factors, and therefore, if this demographic was ultimately chosen, CFL would likely need to revisit these aspects of the company's governance policies. Weak candidates, on the other hand, used this misalignment as a main reason to forgo the over-55 demographic. This discussion point was less valuable, given the board's commitment to changing the direction of CFL in order to save the fitness gyms. Weak candidates also tended to blend their analysis of each age demographic into one discussion; this made it more challenging to provide CFL's board with the requisite amount of both qualitative breadth and depth for each age group.

Quantitatively, strong candidates used the information provided to project the EBITDA that each age demographic target would likely provide to CFL. Strong candidates then discussed the uncertainties involved with the projections (such as the fact that many fitness companies were lowering the cost of their annual memberships, and so, CFL's assumptions on what they could charge for a membership may have been overly optimistic). Finally, strong candidates routinely discussed the annual cash flow required to satisfy each demographic, and highlighted the lower cost associated with the over-55 group as a major advantage, given CFL's limited investment capital. Weak candidates often made mistakes within their earnings projections, such as projecting only revenue without including the applicable expenses or by including only the year-over-year incremental increase/decrease of an expense. Other weak candidates provided overly complicated net present value calculations, and often failed to discuss the outcome of their calculation in relation to the board's objective of improving the company's EBITDA.

AO#3: Should CFL become Zenfit's national distributor?

With respect to CFL's existing agreement with Zenfit, candidates were expected to discuss both of CFL's options: expand the agreement to become Zenfit's exclusive national distributor, or sell the existing Western Canada distribution and video production rights for $9 million. Qualitatively, candidates were expected to identify and discuss a variety of risks (such as the increased number of similar exercise machines that had recently been released) and opportunities (such as Zenfit's new Zentracker machine that was about to released) in relation to becoming Zenfit's exclusive national distributor. Candidates could have also recognized that the practicality of becoming Zenfit's national distributor depended upon which age demographic CFL decided to target at its fitness gyms, given that the over-55 age group preferred not to use Zenfit's equipment. Relative to the potential sale, candidates could have discussed the recent drop in performance of Zenfit's equipment and Zenfit Live, and how this could signal a decline in popularity for Zenfit products. Quantitatively, candidates were expected to revise the projected earnings for the last two years of the existing Zenfit agreement, and compare it to the $9 million offer that CFL had received to sell it. Candidates could have also discussed the likelihood of CFL achieving the minimum annual sales target of $10 million that was part of the proposed agreement to become Zenfit's national distributor.

Most candidates recognized the synergy that existed between the under-40 age demographic and the Zenfit agreement; however, fewer candidates discussed how their recommendation on which demographic to target affected their recommendation on whether to expand or sell the Zenfit agreement. Most candidates recognized that becoming Zenfit's national distributor would be a good way for CFL's brand to gain national exposure without the need to invest more of the company's limited available capital (given that there was no upfront investment associated with becoming Zenfit's national distributor). Most candidates also recognized the possibility of missing the $10 million sales target, but only some candidates identified this as a major risk, given the current downward trend in both the number of Zenfit product sales and the number of subscribers for Zenfit's livestreamed videos. Quantitatively, most candidates attempted to compare the $9 million offer that CFL had received for selling its existing Zenfit agreement to the projected earnings from the last two years of the existing agreement; however, fewer candidates used the downward trend figures that Frank provided in the board dialogue to revise CFL's original earnings projection.

Qualitatively, strong candidates linked their analysis of how to proceed with the Zenfit option with their recommendation on which age demographic to target within CFL's fitness gyms (AO2). These candidates recognized that it did not make strategic sense to expand the Zenfit agreement if the company chose to target the over-55 age demographic. Strong candidates also tended to emphasize the increasing amount of competition that the new Zentracker machine would face, and how that could further reduce CFL's earnings derived from Zenfit product sales. Weak candidates, on the other hand, suggested that the addition of Zenfit's new machine would catalyze the resurgence of Zenfit's sales, without discussing the competition risk. Weak candidates also tended to highlight Zenfit's alignment with CFL's mission, vision, and key success factors as a main reason for becoming the national distributor. This point had less value, given that all the investment options available to CFL had a similar alignment. Some weak candidates suggested that CFL forgo both the option to become Zenfit's national distributor and the opportunity to sell the contract for $9 million. This recommendation lacked value, given that there were only two years left on the existing agreement, and because Zenfit would not allow CFL to renew its current agreement if CFL did not agree to now become the national distributor.

Quantitatively, strong candidates provided a revised earnings projection for the final two years of the existing agreement, given the information provided in the board dialogue. These candidates recognized that the $9 million offer to sell the existing agreement exceeded the projected earnings. Strong candidates also discussed the need to further analyze CFL's ability to meet the minimum $10 million sales target, should CFL decide to become Zenfit's national distributor, given the lack of information provided in the simulation. Weak candidates struggled to provide a valuable quantitative analysis, and often used an improper tool to assess the value of the existing agreement (for example, some weak candidates used the EBITDA multiplier from Appendix II, even though it was stated that the multiplier was for recent sales of fitness and recreation facilities).

AO#4: Should CFL open new climbing facilities or instead sell its current climbing facilities?

Given the successful launch of CFL's first climbing facilities, CFL was considering the addition of six more locations that Brian had identified as suitable for climbing. In addition, CFL had received an offer to sell its existing eight climbing facilities for $12 million. Candidates were expected to analyze, and advise CFL's board on, whether either option was strategically advantageous. Relative to the potential expansion, candidates could have discussed a variety of risks and opportunities, such as the significant advantage of this segment of the industry having less competition in comparison to the fitness gyms, and fitness machines such as Zenfit. Relative to the potential sale, candidates could have discussed how the proceeds could be used to expand and/or secure the company's core business: the fitness gyms. Quantitatively, candidates were expected to calculate the EBITDA generated from the existing climbing facilities and then, using the EBITDA multiplier provided, compare the $12 million offer to sell the climbing facilities to their implied value. Candidates could have also assessed the quantitative strength of the expansion opportunity by comparing the cost of the expansion to the expected EBITDA that it would generate.

Most candidates did a good job of recognizing the early success of the climbing facilities, and the potential to build on their early success by opening additional locations. Most candidates also highlighted Brian as a main driver of the climbing facilities' success. As a risk, most candidates discussed the injuries that the two climbers had suffered at CFL's climbing facilities (both injuries, given the improper use of equipment, were the fault of climbers). Some candidates highlighted this risk as the main reason to sell the climbing facilities, while a better discussion recognized that this risk could be mitigated through the continued use of waiver forms and adherence to the proper safety standards. Quantitatively, most candidates attempted to assess the potential profitability of the expansion plan and the reasonability of the $12 million offer to sell the climbing facilities.

Qualitatively, strong candidates recognized, and discussed, the growth potential of the climbing facilities, given the lack of competition, Brian's ability to provide a satisfying experience for the members, and the growing popularity of climbing across all age demographics. Strong candidates also recognized the brand confusion that had arisen between CFL's fitness gyms and climbing facilities, and suggested ways to mitigate this issue (for example, some candidates suggested that CFL offer a type of membership that allowed access to both the fitness gyms and the climbing facilities). Weak candidates tended to focus on the risks of the climbing facilities and the proposed expansion, without offering potential ways to mitigate those risks. Weak candidates also highlighted the complaints that CFL had received from the members who lost access to the fitness gyms when they were converted into climbing facilities as a reason to forgo the option to open additional locations. These candidates failed to recognize that the proposed expansion did not require the conversion of more fitness gyms, given that the six potential new climbing facilities were not currently CFL fitness gyms.

Quantitatively, strong candidates were better able to assess the reasonability of the $12 million offer to sell the climbing facilities that CFL had received. Strong candidates gave a simple calculation that used the EBITDA multiplier provided to calculate the implied value of the existing eight climbing facilities. That value was then compared to the $12 million purchase offer. Strong candidates also tended to discuss how the potential expansion into new climbing facilities appeared to be a relatively risk-free way to achieve the board's objective of improving the company's EBITDA, or the possibility of opening only one or two new climbing facilities at a time as a way to manage CFL's limited investment capital. Weak candidates tended to provide calculations that contained errors, such as not adding back amortization to the climbing facilities' operating income in order to determine the climbing facilities' EBITDA.

<u>AO#5: Should CFL acquire RJ's Health Clubs Limited?</u>

RJ, a struggling fitness company located in Eastern Canada that shared a similar format to CFL's existing fitness gyms, was up for sale, and CFL's board was considering whether it made strategic sense to acquire it. Candidates were expected to assess whether CFL should pursue the acquisition. Qualitatively, candidates were expected to recognize that RJ offered CFL the opportunity to significantly expand the company's fitness gym operations, and therefore carry out its mission and vision. Candidates were also expected to discuss the significant risk of purchasing a company that appeared to be quickly going out of business. Quantitatively, candidates were expected to assess whether the asking price for RJ was reasonable, in light of RJ's declining EBITDA. Candidates could have also analyzed whether it would be possible for CFL to improve RJ's performance by targeting a specific age demographic.

Most candidates recognized the significant risk of purchasing RJ, given the company's substantial decline in performance that had occurred between 2022 and 2024. Most candidates also attempted to calculate the implied value of RJ by applying the EBITDA multiplier to the company's earnings information. The combination of the above two factors led many candidates to recommend against the acquisition. Few candidates recognized that the performance of RJ could potentially increase, and therefore make the acquisition price of $7.5 million more reasonable, if CFL were to target a specific age demographic (for example, if CFL were to purchase RJ and target the over-55 age demographic, the acquisition of RJ could be a bargain).

Qualitatively, strong candidates recognized that the acquisition would nearly double the number of fitness gyms that CFL would have, and linked that advantage to the potential alleviation of the financial constraint, given that lenders were reluctant to extend debt to fitness companies with fewer than 50 locations. Strong candidates also made the link between the over-55 age demographics' desire for yoga and meditation classes with the fact that RJ was equipped to provide these classes. Weak candidates tended to emphasize the disadvantages of the potential acquisition, such as the fact that RJ's equipment had become outdated, and how that would violate CFL's key success factors. Although this was a valid point, these candidates struggled to incorporate the board's objective of targeting a specific age demographic within their analysis of this opportunity (for example, if the board decided to target the over-55 age demographic, this would necessitate the revision of the company's governance policies). Weak candidates also discussed how the acquisition of RJ would lead to the cannibalization of CFL's current fitness gym members. This point had no value, given that RJ's gyms were located in Eastern Canada whereas CFL's current fitness gyms were in Western Canada.

Quantitatively, most candidates typically attempted to calculate the implied value of RJ, and then compared that value to the asking price for RJ. However, only strong candidates attempted to project RJ's potential future earnings, should CFL purchase RJ and then target a specific age demographic. These candidates discussed how the acquisition of RJ offered CFL the opportunity to meet the board's objective of improving the company's EBITDA if CFL was able to successfully target the over-55 age demographic within RJ's fitness gyms. Weak candidates tended to base their analysis on RJ's existing earnings information without analyzing whether it could be possible to improve their performance.

AO#6: Rosa's replacement on CFL's board

Given the departure of Rosa, candidates were expected to discuss whether either Louisa Rice or Albert Fong would be a suitable replacement as a CFL board member.

Most candidates did a good job of discussing the advantages and disadvantages of each potential replacement relative to CFL's existing mission, vision, and other governance policies. However, only the strong candidates linked their analysis of which replacement would be the most suitable in light of CFL's objective of focusing on either the under-40 or over-55 age demographic. Strong candidates integrated their recommendation of which age demographic to focus on with their analysis of which replacement would be the most suitable. For example, strong candidates recognized that Louisa's attributes would be the most beneficial to CFL if the company chose to target the younger demographic, whereas Albert would likely be the better choice if CFL targeted the older demographic. Weak candidates failed to link their discussion of which replacement would be the best choice with the broader, entity-level considerations, such as CFL's need to target a specific demographic. In addition, a common mistake that weak candidates made was to discuss how the sale of Rosa's shares would provide CFL with additional cash when, in reality, Rosa would have been the recipient of the proceeds and not CFL.

Overall

The focus of SO#2 was on the candidate's ability to integrate elements of the company's global situation (such as the increase in competition within the fitness gym market, and the board's objective of increasing the company's EBITDA) with their qualitative and quantitative analysis of each AO, and to consider how the viability of each AO would be affected by the main strategic question of the simulation: which age demographic to target within CFL's fitness gyms.

Most candidates addressed each of the strategic options available to CFL; however, many of the weak candidates took an "issue by issue" approach, and therefore failed to make the important links between the various aspects of each alternative (for example, weak candidates typically did not incorporate the preferences of each age demographic within their analysis of any AO beyond AO2). Conversely, strong candidates recognized that these preferences could have impacted the relative strength of the other strategic options available (for example, strong candidates recognized that becoming the national distributor for Zenfit would likely appeal to under-40 age demographic, given the group's preference for high-tech equipment).

Strong candidates provided a well-balanced qualitative discussion that outlined both the advantages and disadvantages of each strategic option, and made more relevant links back to the company's situational analysis (SO#1). Weak candidates tended to make numerous links back to CFL's current corporate governance policies (namely, the mission, vision, and key success factors that were outlined in Capstone 1). These candidates had a tougher time adapting their analysis to the specifics of the simulation, such as how the industry had shifted, given the significant increase in competition, and how that increase in competition was rapidly driving the performance of CFL's fitness gyms downward. Most candidates did a good job of identifying the AO-specific case facts that would impact the viability of each strategic option, but weak candidates struggled to provide the applicable implications of those case facts. Other weak candidates simply listed case facts without attempting to explain why those facts were important to the decision.

Most candidates attempted to analyze each strategic option from a quantitative perspective (except for AO6, which had no quantitative element). Strong candidates routinely provided straightforward calculations that addressed each aspect of the alternative that was being analyzed (for example, strong candidates provided a quantitative analysis for both the proposed expansion plan and the $12 million purchase offer for the climbing facilities). Strong candidates routinely tied their quantitative assessments back to the company's EBITDA objective. Weak candidates sometimes failed to provide a complete quantitative analysis for some of the strategic options (for example, some weak candidates failed to analyze the reasonability of the $9 million offer that CFL had received to sell Zenfit). Weak candidates were also more likely to provide overly complicated calculations that contained many errors, and that failed to address the board's objective of improving the company's EBITDA.

SO#3 (Conclude and Advise)

For each of the strategic options available to CFL, candidates were expected to provide recommendations that were consistent with their analyses. Candidates were also expected to provide an integrative conclusion that linked together the analysis and recommendations they provided for each AO in a cohesive and sensible way. Candidates could have accomplished this in a variety of ways. The most common way to integrate was through a discussion of how the candidate's recommendation in AO2 (which age demographic to target at the company's fitness gyms) impacted their analysis and recommendations of whether to proceed with the other strategic options available to the company. For example, many candidates, after recommending that CFL target the under-40 age group, went on to discuss how the Zenfit national distributor proposal would be in strategic alignment with that recommendation, given the younger age demographic's desire for high-tech gym equipment that integrated well with wearable fitness devices. Other candidates, after recommending that CFL target the over-55 age group, went on to discuss how Louisa Rice was a less suitable replacement for Rosa, given her intense approach to fitness, which did not align with the preferences of the older demographic. Candidates could have also provided integration by describing how CFL could finance the recommended investments through selling either the company's existing Zenfit agreement or the climbing walls, or by acquiring RJ and therefore gaining the potential to access further debt financing.

Strong candidates provided responses that included several integrative elements, and an overall conclusion that did not violate the company's cash availability. Strong candidates also provided conclusions that made good strategic sense when taken as a whole. Weak candidates struggled to provide conclusions that would have resulted in a sensible overall strategy direction. For example, some weak candidates recommended targeting the over-55 age demographic as well as becoming Zenfit's national distributor; this type of conclusion had no integrative value, given the dislike that the over-55 group had for Zenfit's equipment. Weak candidates also had a difficult time recognizing that CFL could use the proceeds from selling either the Zenfit agreement or the climbing walls to increase the company's EBITDA to a greater degree, relative to what those aspects of CFL's current business presently offered. For example, many candidates recommended against the sale of the Zenfit agreement because that would reduce the company's EBITDA and therefore violate the board's objective. These candidates did not recognize that the proceeds from either potential sale could have been redeployed in a more advantageous way.

SO#4 (Communication)

Most candidates approached their response in a coherent and organized fashion. Only a few candidates struggled to effectively communicate their ideas. These candidates tended to use poor sentence structure, confusing syntax, and an unorganized response approach.

SO#5 (Overall Assessment)

Overall, candidates were expected to meet the minimum acceptable standards in each of the four summative opportunities in order to obtain a "Pass" on the Day 1 linked case. Candidates also had to demonstrate a minimum level of numeracy skills on the quantitative elements of the simulation.

For each major issue, candidates were expected to perform a sufficient level of analysis, and to then provide a recommendation that was consistent with their analyses and that did not violate CFL's cash availability. The board sought evidence that candidates incorporated the important elements of Capstone 1, as well as the main elements of this simulation's situational analysis, into their analysis of the major issues. Candidates were also expected to provide a reasonable amount of integration between the strategic options that were presented in the simulation.

BOARD OF EXAMINERS' COMMENTS ON DAY 1 (CFL VERSION 2)

Paper/Simulation:	Day 1 – Linked Simulation, CFL V2 (on September 2023 CFE)
Estimated time to complete:	240 minutes
Simulation difficulty:	Average
Competency Map coverage:	N/A; Enabling Skills

Examiners' comments by Summative Assessment Opportunity (SO)

SO#1 (Situational Analysis)

Candidates were expected to highlight the factors, both internal and external to CFL, that could have influenced the strategic decisions presented in the simulation. From the strategic options available to the company in Capstone 1, CFL had chosen to convert eight of its fitness facilities into indoor climbing facilities, and had also accepted Amanda's PurCafés proposal to open health food cafés within five of CFL's fitness facilities. Both of these investments had proven to be successful so far, and had helped improve CFL's financial situation. Two other factors that had contributed to CFL's improved performance were higher-quality fitness classes and an increase in the company's member retention rates. Since Capstone 1, the company had also revised both its mission and vision statements. In addition, the board's main objectives had also changed since Capstone 1, given the board's desire to step back from the active involvement in CFL's day-to-day operations within roughly five years. In order to protect the company's annual dividend, which the board members planned to use to fund their retirements, the board wanted to make low-risk investments that were simple to operate and that provided a stable and reliable source of revenue. So, although the board wanted to both increase and diversify the company's sources of revenue, and increase the company's EBITDA, it was important to limit the amount of risk that any new strategic investment would present to the company's earnings. Therefore, as part of their analysis within SO#2, candidates were expected to discuss the relative amount of risk associated with each strategic option, and to tailor their recommendations in a way that would best ensure that the company's annual dividend would not be put in jeopardy. In addition to the importance of managing the company's investment risk, the company was also faced with a limited amount of investment capital, given that CFL had only $6.5 million of cash available for investment and no access to further debt financing. Candidates were rewarded when they made relevant links between their situational analysis and their analysis of the strategic alternatives in SO#2, and recommendations in SO#3.

Most candidates provided an adequate summary of CFL's internal and external situation at the beginning of their report. Candidates typically included an updated SWOT analysis that highlighted the changes in the company's situation that had occurred since Capstone 1, and identified the board's main objectives to be considered in relation to the strategic options presented in the simulation. Despite recognizing the company's main objectives, many candidates failed to adequately discuss the various risks associated with each strategic investment option, and potential ways to mitigate these risks.

Strong candidates provided a situational analysis that tended to highlight the most relevant macro-level factors of CFL's existing internal and external business environment. Strong candidates also recognized that, given the board's intention to step back from the company's day-to-day operations, CFL would soon be in a state of transition, and any strategic investments made would therefore need to align with the company's future governance environment. These candidates highlighted the two main restrictions that CFL faced when deciding which strategic alternatives to pursue in SO#2: the company's limited investment capital; and the board's impending retirement. Strong candidates would then consistently link their analysis of each strategic option to how that option would be affected by these restrictions.

Weak candidates tended to simply list CFL's revised mission and vision, and the company's core values and key success factors from Capstone 1 without highlighting which of those aspects would play an emphasized role in their analysis, based on the information provided in the simulation. Other weak candidates simply restated the case facts that were provided in the simulation without identifying which of those items would have the most influence on their decision-making process. Weak candidates also struggled to link their analysis of the strategic options in SO#2 and SO#3 to the most relevant situational elements presented in the simulation, and instead attempted to link their discussions and recommendations to less relevant aspects of CFL's governance policies (such as by making weak links between aspects of each strategic decision, and how well they did or did not fit with CFL's mission and vision statements). Links to the mission and vision statement were less valuable because every strategic option presented in the simulation aligned quite well with them.

SO#2 (Analysis of the Issues)

Candidates were expected to analyze five strategic alternatives, both qualitatively and quantitatively. Candidates were also expected to integrate the key macro-level aspects of CFL's internal and external situation within their analysis of each strategic alternative (such as the board's desire to make low-risk investments in projects that were simple to operate, and that provided a reliable source of revenue).

AO#2: Acquire Iron Depot?

Candidates were presented with whether CFL should acquire Iron Depot, an exercise equipment outlet store that sold both new and used exercise equipment at reduced prices. The information required to analyze this strategic alternative was provided in the Appendix I board meeting dialogue, as well as in Appendix II. Qualitatively, candidates were expected to assess whether Iron Depot's business model aligned with the board's objective to invest in low-risk projects that were easy to operate. Quantitatively, candidates were expected to assess whether the asking price for Iron Depot was reasonable, given what similar companies had recently sold for, and whether the acquisition would help CFL reach the board's objectives of increasing the company's revenue and EBITDA. Candidates could have also discussed how Iron Depot's supplier contracts would have offered CFL a 20% discount on equipment sales, which would have benefited the company's core operations of operating fitness facilities.

Most candidates recognized the main risks associated with the acquisition, such as the fact that Iron Depot's current owner, who was active in the company's management, planned to retire shortly after the sale was made, and that CFL did not have any experience in operating a retail business; however, fewer candidates recognized that these risks could be mitigated by hiring a senior manager with retail experience. Most candidates also recognized that the acquisition would help CFL diversify its sources of revenue and that the acquisition aligned well with CFL's revised mission and vision statements. In addition, most candidates recognized that the acquisition aligned well with the recent increase in demand for fitness products and the popularity of working out from home. Quantitatively, most candidates attempted to calculate the value of Iron Depot and then assess whether the asking price of $10 million was reasonable by comparing the calculated value of Iron Depot's business to the asking price.

Strong candidates recognized that the acquisition aligned well with the board's objective to make low-risk investments that provide a reliable source of revenue. These candidates recognized that Iron Depot's history indicated the relative safety of the investment, given that Iron Depot was 25 years old and had only suffered one outlet closure, which appeared to be due to opening an outlet in a town whose population was too small to support an Iron Depot location. Further, these strong candidates recognized that Iron Depot's business model was quite basic, and how that would help mitigate the risk associated with the impending retirement of Iron Depot's current owner. Quantitatively, strong candidates correctly calculated Iron Depot's normalized EBITDA by adjusting for the expected change in Iron Depot's salary expense, and the one-time expense incurred to hire an investment bank and accounting firm, and used the EBITDA multiplier provided to calculate the implied value of Iron Depot's business. Strong candidates would also calculate the amount of money that CFL would save on the company's annual equipment purchases if the equipment was purchased through Iron Depot's suppliers.

Weak candidates tended to highlight the closure of Iron Depot's North Bay location as a main reason not to invest in Iron Depot, even though the circumstances that resulted in this location's closure were clearly explained and could easily be managed by CFL, to ensure that it does not occur again. Weak candidates also tended to highlight CFL's lack of experience in operating this type of business as another main reason to not invest in Iron Depot. Rather than attempt to mitigate this risk and therefore move forward with an attractive investment, weak candidates tended to recommend avoiding the investment altogether. Weak candidates also highlighted the need to hire a senior manager as a reason to forgo this investment, even though CFL's board intended to use senior managers to operate CFL after the board's retirement. Quantitatively, when weak candidates attempted to determine the value of Iron Depot's business, they did not normalize Iron Depot's EBITDA for the expected changes in expense, and therefore arrived at an inaccurate valuation. Weak candidates also typically missed calculating, or commenting on, how Iron Depot's discount with its supplier contracts would impact CFL's core business.

AO#3: Sign hotel gym management contract with Sunnyside Hotels?

Candidates were presented with whether CFL should sign a management contract with Sunnyside Hotels to design and operate a small but well-equipped gym in each of Sunnyside's seven hotels. The information required to analyze this strategic alternative was provided in the Appendix I board meeting dialogue, as well as in Appendix III. Qualitatively, candidates were expected to recognize that, aside from the limited space available to design the hotel gyms, this strategic investment aligned well with CFL's core competencies. Candidates were also expected to recognize that one key feature of the management contract was unknown: whether CFL or Sunnyside would be held liable if someone was injured while using the hotel gym. Given this potential risk, candidates were expected to recommend that CFL clarify this aspect of the arrangement, and also obtain an adequate amount of insurance, to indemnify the company against any possible accidents. Quantitatively, candidates were expected to analyze the potential profitability of the management contract, using a reasonable tool such as a net present value calculation or a payback period calculation, and discuss whether the contract would help CFL reach the board's objectives of increasing the company's revenue and EBITDA.

Most candidates recognized how this strategic investment could boost the performance of CFL's primary business, the company's fitness facilities, given the free marketing that would result from calling the hotel gyms "Sunnyside Gyms by CanDo Fitness." Most candidates also recognized that it would be a challenge to design the hotel gyms, given the limited available space within each hotel. Most candidates recognized the risk associated with someone becoming injured while using the hotel gyms; however, only strong candidates recognized that there were ways to mitigate this risk, such as through obtaining the requisite amount of insurance. Quantitatively, most candidates attempted to analyze the profitability of the management contract through the use of a net present value calculation.

Strong candidates recognized that, given the management contract's alignment with CFL's core competencies, this strategic investment opportunity aligned well with the board's objective of investing in projects that were simple to operate. Moreover, these candidates recognized that the company would be able to effectively manage and mitigate the risks involved in the project and therefore, the board's desire to invest in low-risk investments would also be satisfied through entering into the management contract. Strong candidates also recognized that the logistics involved in replacing the equipment in the hotel gyms every two years would be made easier if CFL acquired Iron Depot, given that the used equipment could be sold through Iron Depot's outlet. Quantitatively, strong candidates provided a reasonable net present value calculation that included the equipment repurchase cost in Years 2 and 4, and concluded that, based on the information provided, the project appeared to be profitable. Strong candidates also recognized that the management contract aligned well with the board's quantitative objectives, given that the management contract provided CFL with a fixed amount of revenue each year.

Weak candidates struggled to identify the more relevant qualitative aspects of this potential investment, and tended to focus their discussion on less relevant aspects such as the proposal's alignment with CFL's revised mission and vision statements, and the company's core values. Weak candidates also highlighted the need to hire a senior manager as a reason to forgo this investment, even though CFL's board intended to use senior managers to operate CFL after the board's retirement. Quantitatively, although most weak candidates attempted a net present value analysis, their calculations often contained errors, such as not including the cost to purchase new equipment every two years and/or the salvage value of the used equipment that would be sold every two years. Weak candidates also tended not to discuss the results of their quantitative analysis in a meaningful way (such as by linking their analysis to one of the objectives provided by CFL's board), and would instead simply comment that, because the NPV calculation is positive, CFL should proceed with the investment.

AO#4: Engage Rise Edustream to help create and distribute streaming fitness videos?

Candidates were presented with whether CFL should use the services of RiseEd to produce and distribute fitness videos via an online streaming platform. The information required to analyze this strategic alternative was provided in the Appendix I board meeting dialogue, as well as in Appendix IV. Qualitatively, candidates were expected to recognize the significant risks and uncertainties associated with this project, and therefore the misalignment between the proposal and the board's stated objectives. Quantitatively, candidates were expected to perform a sensitivity analysis on the three-year projection provided by RiseEd. Candidates were also expected to discuss RiseEd's proposed fee structure and how, even if the streaming service attracted very few subscribers, CFL would still be required to pay RiseEd a significant fee.

Most candidates recognized that RiseEd's proposal aligned well with the increased popularity of home workouts, and the fact that the demand for streaming fitness videos had grown, and that this growth was expected to continue for the foreseeable future; however, fewer candidates highlighted the significant amount of competition that CFL would face within the streaming fitness video market. Most candidates also recognized that this project offered CFL the potential to grow the company's brand, given that the videos would use CFL's brand name; however, fewer candidates recognized that this facet of the project also represented a risk to CFL if the quality of the videos fell below the expectations of the videos' users. Quantitatively, most candidates attempted to project the annual operating income that CFL could expect to earn through the project.

Strong candidates recognized the inherent complexities and uncertainties of this investment option, and therefore the misalignment between the proposal and the board's main objectives. For example, strong candidates recognized that this venture's success would greatly depend on the number of subscribers that CFL could attract to the streaming platform, and that this outcome was far from assured, given the number of existing competitors that offered a similar service and CFL's general lack of experience in this type of business. Strong candidates also highlighted certain features of the proposal, such as the need for CFL to provide the platform's subscribers with customer support, as a complex element that violated the board's objective to invest in projects that were simple to operate. Quantitatively, strong candidates recognized that the accuracy of the projection provided was questionable, given that it was compiled by RiseEd (who had a vested interest in moving forward with the project). As a result, strong candidates performed a sensitivity analysis on the projection, and concluded that the profitability of the proposal was far from assured, and that, even if the platform failed to attract an adequate amount of subscribers, CFL would still be required to pay RiseEd an annual fee.

Weak candidates tended to miss the significant risks associated with this investment, and instead focused their discussion on the industry trends that indicated the growing popularity of streaming fitness videos. Weak candidates also discussed the possibility of CFL developing its own piece of unique equipment in order to compete with the other fitness companies with streaming services; these candidates failed to recognize that developing fitness equipment violated the board's objective of investing in projects that were simple to operate. Quantitatively, weak candidates tended to provide a six-year income projection based on the numbers provided by RiseEd, and concluded that the investment appeared to be highly profitable without questioning the accuracy of the information provided, given its source. Weak candidates also failed to perform a sensitivity analysis for the investment, and therefore missed the risk that attracting fewer subscribers may cause the project to lose money.

<u>AO#5: Develop and operate physiotherapy clinics?</u>

Candidates were presented with the fact that CFL had identified eight CFL fitness facilities that had underutilized space. To make better use of this space, the company had identified two potential investment alternatives, physiotherapy clinics and PurCafés. Candidates were expected to analyze and conclude on which option better aligned with the company's existing business and the board's stated objectives. Information on the physiotherapy clinics was provided in Appendix V, and information on the PurCafés was provided on Appendix VI. As a part of this decision, candidates were expected to analyze whether CFL should develop and operate a physiotherapy clinic within eight of the company's existing gyms. Qualitatively, candidates were expected to recognize that offering physiotherapy, a highly specialized and technical service, fell well outside of the board's preference for investing in projects that were simple to operate. Quantitatively, candidates were expected to calculate a sensitivity analysis for the potential clinics' income at each level of clinic utilization, and recognize that the project's financial success greatly depended on achieving a high level of utilization.

Most candidates recognized that there appeared to be an increasing need for physiotherapy services, given the increase in exercise-related injuries, and that this strategic investment would allow CFL to align the company with this increase in demand. Most candidates also recognized how well this strategic investment aligned with the company's mission, vision, and core values, and how the opportunity could provide CFL with a competitive advantage; however, fewer candidates recognized that this outcome depended on the quality of the service provided and that, if the quality was poor, the company's reputation could be harmed. Quantitatively, most candidates attempted to calculate a sensitivity analysis on the project's potential income, and provided a payback period calculation at the various levels of clinic utilization.

Strong candidates highlighted the risks and uncertainties associated with this strategic investment option. For example, strong candidates recognized that, in order for the investment to be successful, the clinics would need to be marketed aggressively and staffed with highly-qualified physiotherapists. Therefore, given these complexities, as well as CFL’s general lack of experience with offering this type of service, strong candidates recognized that this strategic investment option did not align well with the board objectives of making low-risk investments with reliable earnings. Strong candidates also recognized the elevated risk associated with this strategic investment, given that its success largely depended on Nav Srinivasan and his ability to develop and operate the clinics effectively. Quantitatively, strong candidates provided a sensitivity analysis on the potential physiotherapy clinics’ annual earnings, based on the possible levels of clinic utilization, and then went on to interpret and discuss the results of their calculations. Strong candidates recognized that it would likely take time for the clinics to reach full utilization, given that CFL would need to attract new customers through an aggressive marketing campaign. Moreover, strong candidates recognized that, even with a strong and successful marketing campaign, the full utilization of the clinics also relied on the quality of service that customers received and the reputation of the clinics, something that was largely outside of the board’s control, given the investment’s reliance on Nav, as well as the board’s general lack of experience in providing this type of highly-technical service. Given that one of the board’s objectives was to invest in projects with a stable and reliable source of revenue, strong candidates recommended against this investment.

Weak candidates tended to link this strategic investment option to the company’s mission, vision, and core values, and often highlighted the investment’s potential to offer CFL a competitive advantage, without recognizing its inherent risks and uncertainties. Quantitatively, weak candidates calculated the potential physiotherapy clinics’ annual earnings based on the three possible levels of clinic utilization, but failed to recognize how sensitive the investment’s EBITDA was to the different levels of utilization. Rather than discussing whether the investment fit with the board’s preference for stable and reliable revenue, weak candidates tended to highlight the high earning potential of the investment if the clinics reached full utilization. Rather than question whether reaching full utilization was realistic, weak candidates tended to base their recommendation on the clinics’ high earnings and low payback period that would result when the clinics reached full utilization.

AO#6: Open additional PurCafés?

Candidates were presented with the fact that CFL had identified eight CFL fitness facilities that had underutilized space. To make better use of this space, the company had identified two potential investment alternatives, physiotherapy clinics and PurCafés. Candidates were expected to analyze and conclude on which option better aligned with the company's existing business and the board's stated objectives. Information on the physiotherapy clinics were provided in Appendix V, and information on the PurCafés was provided in Appendix VI. As part of this decision, candidates were expected to analyze whether CFL should expand the PurCafés arrangement with Amanda by opening a new café within eight of the company's existing gyms. Qualitatively, candidates were expected to recognize that this option had a significant advantage over the physiotherapy option, given that CFL's existing PurCafés had proven to be successful and were helping to improve the fitness facilities' retention rates. Candidates were also expected to comment on Amanda's workload, and whether she had overextended herself. Quantitatively, candidates were expected to calculate the incremental increase in earnings that CFL could expect if the company opened the additional cafés, and then compare that figure to the expected earnings of the physiotherapy clinic alternative.

Most candidates recognized the risk associated with Amanda's workload, which already appeared to be causing issues within the existing five PurCafés. Most candidates also recognized that Amanda's apparent overwork could be the cause of the recent complaints that CFL had received about the decline in the service quality of the cafés. In addition, most candidates recognized how well this strategic investment aligned with the company's mission, vision, and core values, and the fact that the expansion aligned well with the increasing demand for nutritious food options. Quantitatively, most candidates attempted to calculate the expansion's expected profitability, and provided a payback period calculation for the investment's upfront capital cost.

Strong candidates highlighted the fact that, compared to the physiotherapy clinic option, this option better aligned with the board's objective to invest in low-risk projects, given that the original five PurCafés were already operating and profitable. Strong candidates also recognized that operating the PurCafés was likely far less complicated than the physiotherapy clinics, given the highly technical and specialized nature of physiotherapy, and because CFL already had experience with operating the cafés. Stronger candidates recognized that Amanda's workload is high, but recommended that CFL's board meet with Amanda to discuss how she intended to operate the new PurCafés locations, given her increasing workload, and to gain confidence in Amanda's ability to effectively expand these operations before agreeing to the expansion. Quantitatively, strong candidates calculated the incremental increase in earnings that CFL could expect if the company opened the additional cafés, and then compared that figure to the expected earnings of the physiotherapy clinic alternative. These candidates recognized that the earning potential of the new PurCafés rivaled that of physiotherapy clinics, even when the physiotherapy clinics were close to full utilization. Given that comparison, as well as the board's objective of investing in projects with stable earnings, strong candidates recognized that the PurCafés expansion was a better fit for CFL.

Weak candidates tended to focus their analysis on the more superficial aspects of the investment, such as the alignment between offering healthy food and the company's mission, vision, and core values. Weak candidates also tended to focus their analysis on Amanda's apparent overwork, and recommended that CFL forgo the PurCafés expansion because of Amanda's workload. Although Amanda's workload was certainly a concern, she had also proven herself to be a capable and valuable addition to CFL's business, and there were likely solutions to address her workload. Quantitatively, weak candidates had a hard time providing an incremental earnings analysis of the potential expansion, and often missed including relevant aspects of the expansion within their calculations (such as the required new lease, or the increase in Amanda's compensation). Weak candidates also did not compare the results of their calculation for the PurCafés expansion to their results of the physiotherapy option, which made their analysis less useful in helping the board decide which option was most suitable.

<u>Overall</u>

The focus of SO#2 was on the candidate's ability to integrate the board's stated investment objectives within both their quantitative and qualitative analyses. Given that the board planned to reduce their involvement in the day-to-day operations of the company, and that they planned to rely on the dividends they received from CFL to fund their retirements, it was imperative that candidates recognize and consider how well each investment option aligned with the board's preference for safe, stable, and reliable projects. Candidates were also expected to consider how well each strategic investment option aligned with CFL's existing business, and whether any of the investment options would benefit the company's existing operations.

Most candidates addressed all the strategic options available to CFL; however, some candidates did not provide a fulsome discussion for the physiotherapy clinics and/or the PurCafés expansion option. Often, these candidates provided a very detailed situational analysis, and therefore did not allow themselves sufficient time to respond more fully to the strategic options that came toward the end of the simulation. Most candidates also provided a sufficient quantitative analysis, which was expected, given that the calculations required were basic in nature.

Within SO#2, there were two main differentiating factors between strong and weak candidates. First, in connection with the board's stated investment objectives, strong candidates routinely discussed the risks associated with each investment, and whether the investment was likely to be easy to operate and would generate a reliable and stable source of revenue. Weak candidates missed the significance of the board's objectives, and either largely failed to link their analysis to the objectives, or did so in a superficial way. For example, some weak candidates would state that a certain investment was low risk and therefore met the board objectives, without explaining what made the investment low risk or what mitigating factors could be used to lower the investment risk. Second, strong candidates routinely provided the implications (the "so what?") of each case fact that they included within their analysis, whereas weak candidates tended to simply list the case facts they thought were relevant to each AO, without explaining the importance of those case facts and what impact they would have on CFL's decision of whether to make the investment.

SO#3 (Conclude and Advise)

Candidates were expected to conclude on each issue analyzed, and to provide an overall conclusion that integrated the macro-level considerations into a cohesive and logical recommendation. A logical overall recommendation was one that discussed and integrated the board's main investment objectives, as well as one that respected the amount of capital the company had available for strategic investment. These conclusions and recommendations were expected to be consistent with the candidate's analyses.

Almost all candidates provided issue-by-issue conclusions and an overall recommendation. Strong candidates formed a cohesive strategy for how the company should allocate its limited investment capital, given the fact that the board was planning to reduce their involvement in the day-to-day operations of CFL, and that the board planned to use the dividends they would receive from CFL to fund their retirements. Strong candidates also discussed the interrelationships between the investment recommendations they made and CFL's existing and potential future operations. For example, strong candidates recognized that, by investing in Iron Depot, the company's annual cost of purchasing new exercise equipment would likely fall, given that CFL could use Iron Depot's supplier contracts to purchase equipment at a 20% discount. Strong candidates also recognized that the Iron Depot investment would allow the company to more easily purchase and resell the equipment necessary to equip the hotel gyms that CFL was considering in relation to the agreement with Sunnyside Hotels.

Weak candidates did not link their recommendations for each strategic option together into a cohesive overall strategy. Instead, weak candidates tended to make their recommendations for each strategic option in isolation from their other recommendations, and did not go further to consider some of the macro-level considerations, such as the board's investment objectives or the board's desire to reduce their involvement in the day-to-day operations of CFL.

SO#4 (Communication)

Most candidates approached their response in a coherent and organized fashion. Only a few candidates struggled to effectively communicate their ideas. These candidates tended to use poor sentence structure, confusing syntax, and an unorganized response approach.

SO#5 (Overall Assessment)

Overall, candidates were expected to meet the minimum acceptable standards in each of the four summative opportunities in order to obtain a "Pass" on the Day 1 linked case. Candidates also had to demonstrate a minimum level of numeracy skills.

For each major issue, candidates were expected to provide a sufficient level of analysis, and then to provide a recommendation that was consistent with their analyses. Candidates were also expected to provide a reasonable amount of discussion on how well each strategic investment alternative aligned with both the board's quantitative and qualitative objectives. Finally, the board sought evidence that candidates incorporated the important elements of Capstone 1, as well as the main elements of this simulation's situational analysis, into their analysis of the major issues

APPENDIX I

CPA COMMON FINAL EXAMINATION REFERENCE SCHEDULE

CPA COMMON FINAL EXAMINATION REFERENCE SCHEDULE

Present Value of Tax Shield for Amortizable Assets

Present value of total tax shield from CCA for a new asset acquired after November 20, 2018, and before January 1, 2024, other than those eligible for immediate expensing.

$$= \frac{CdT}{(d+k)}\left(\frac{1+1.5k}{1+k}\right)$$

Notation for above formula:
C = net initial investment
T = corporate tax rate
k = discount rate or time value of money
d = maximum rate of capital cost allowance

Selected Prescribed Automobile Amounts

Item	2022	2023
Maximum depreciable cost — Class 10.1	$34,000 + sales tax	$36,000 + sales tax
Maximum depreciable cost — Class 54	$59,000 + sales tax	$61,000 + sales tax
Maximum monthly deductible lease cost	$900 + sales tax	$950 + sales tax
Maximum monthly deductible interest cost	$300	$300
Operating cost benefit — employee	29¢ per km of personal use	33¢ per km of personal use
Non-taxable automobile allowance rates		
— first 5,000 kilometres	61¢ per km	68¢ per km
— balance	55¢ per km	62¢ per km

Individual Federal Income Tax Rates

For 2022:

If taxable income is between	Tax on base amount	Tax on excess
$0 and $50,197	$0	15%
$50,198 and $100,392	$7,530	20.5%
$100,393 and $155,625	$17,820	26%
$155,626 and $221,708	$32,180	29%
$221,709 and any amount	$51,344	33%

For 2023:

If taxable income is between	Tax on base amount	Tax on excess
$0 and $53,359	$0	15%
$53,360 and $106,717	$8,004	20.5%
$106,718 and $165,430	$18,942	26%
$165,431 and $235,675	$34,208	29%
$235,676 and any amount	$54,579	33%

Selected indexed amounts for purposes of computing income tax

Personal tax credits are a maximum of 15% of the following amounts:

Item	2022	2023
Basic personal amount, and spouse, common-law partner, or eligible dependant amount for individuals whose net income for the year is greater than or equal to the amount at which the 33% tax bracket begins	$12,719	$13,521
Basic personal amount, and spouse, common-law partner, or eligible dependant amount for individuals whose net income for the year is less than or equal to the amount at which the 29% tax bracket begins	14,398	15,000
Age amount if 65 or over in the year	7,898	8,396
Net income threshold for age amount	39,826	42,335
Canada employment amount	1,287	1,368
Disability amount	8,870	9,428
Canada caregiver amount for children under age 18, and addition to spouse, common-law partner, or eligible dependant amount with respect to the Canada caregiver amount	2,350	2,499
Canada caregiver amount for other infirm dependants age 18 or older (maximum amount)	7,525	7,999
Net income threshold for Canada caregiver amount	17,670	18,783
Adoption expense credit limit	17,131	18,210

Other indexed amounts are as follows:

Item	2022	2023
Medical expense tax credit — 3% of net income ceiling	$2,479	$2,635
Old age security repayment threshold	81,761	86,912
Annual TFSA dollar limit	6,000	6,500
RRSP dollar limit	29,210	30,780
Lifetime capital gains exemption on qualified small business corporation shares	913,630	971,190

Prescribed interest rates (base rates)

Year	Jan. 1 – Mar. 31	Apr. 1 – June 30	July 1 – Sep. 30	Oct. 1 – Dec. 31
2023	4	5	5	
2022	1	1	2	3
2021	1	1	1	1

This is the rate used for taxable benefits for employees and shareholders, low-interest loans, and other related-party transactions. The rate is 4 percentage points higher for late or deficient income tax payments and unremitted withholdings. The rate is 2 percentage points higher for tax refunds to taxpayers, with the exception of corporations, for which the base rate is used.

Maximum capital cost allowance rates for selected classes

Class	Rate	Additional information
Class 1	4%	For all buildings except those below
Class 1	6%	For buildings acquired for first use after March 18, 2007, and ≥ 90% of the square footage is used for non-residential activities
Class 1	10%	For buildings acquired for first use after March 18, 2007, and ≥ 90% of the square footage is used for manufacturing and processing activities
Class 8	20%	
Class 10	30%	
Class 10.1	30%	
Class 12	100%	
Class 13	N/A	Straight line over original lease period plus one renewal period (minimum 5 years and maximum 40 years)
Class 14	N/A	Straight line over length of life of property
Class 14.1	5%	For property acquired after December 31, 2016
Class 17	8%	
Class 29	50%	Straight-line
Class 43	30%	
Class 44	25%	
Class 45	45%	
Class 50	55%	
Class 53	50%	
Class 54	30%	

The CPA certification program prepares future CPAs to meet the challenges that await them. For more information on the qualification process, the common final examination (CFE), and the specific education requirements for your jurisdiction, contact your provincial/regional CPA body.

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