

TREASURER'S REPORT

On an annual basis, as required by the Municipal Act, the City prepares and publishes an annual financial statement that consolidates all of the operations for which the City is responsible. The consolidated financial statements are intended to outline to the public, the City's debenture holders and the credit rating agencies how the revenues raised by the City during the previous year were spent and to describe the state of the City's finances at the end of the fiscal year.

To ensure that the consolidated financial statements have integrity and can be relied upon, they are audited by the City's auditor Ernst & Young LLP. The consolidated financial statements must be prepared in accordance with the generally accepted accounting principles as set by the Canadian Institute of Chartered Accountant's (CICA) Public Sector Accounting Board (PSAB).

The Consolidated Financial Statements encompass the following individual statements:

| Name | Purpose |
|--|--|
| Consolidated Statement of Financial Position | Provides a summary of the City's financial assets and liabilities (the net resources the City has for future services and/or what future revenues need to be raised to pay for past transactions) |
| Consolidated Statement of Financial Activities | Outlines funds raised by the City in the year and what those funds were used for – this statement reflects the combined operations of the operating, capital, reserve and reserve funds for the City and its consolidated entities |
| Consolidated Statement of Cash Flows | Summarizes how the City's cash position changed during the year by highlighting the City's sources and uses of cash |
| Analysis of Current Operations | Outlines funds raised by the City in the year for current operations and what those funds were used for and how they compared to the 2005 Budget |
| Analysis of Capital Operations | Outlines funds raised by the City in the year for capital operations and what those funds were used for and how they compared to the 2005 Budget |
| Analysis of Reserves and Reserve Funds | Summarizes funds raised by the City in the year for reserve funds and what those funds were used for and how they compared to the 2005 Budget |

The consolidated financial statements combine the financial results of the City's departments with the financial results of the agencies, boards, commissions and government business enterprises that the City effectively controls. There are 88 entities that are included in the consolidated financial statements and these are listed in note 1 to the consolidated financial statements. The remaining notes to the consolidated financial statements provide further detail about the City's financial results and are an integral part of the statements.

Under PSAB rules, only the Consolidated Statement of Financial Position, Consolidated Statement of Financial Activities and Consolidated Statement of Cash Flow are required statements. However, to aid the reader's understanding of the consolidated financial statements, schedules have been prepared for current operations, capital operations and reserves and reserve funds.

The Consolidated Statement of Financial Position is sometimes referred to as the municipal equivalent of the private sector's balance sheet. However, there is one important distinction in that the net book value of the City's physical or "fixed" assets (land, infrastructure, buildings and equipment) are not disclosed. Instead, this statement

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focuses on the City's financial assets and financial liabilities. The difference between the two is the City's net liabilities position and this represents the net amount that must be financed in future budgets.

The City's net liabilities are broken down in the "Municipal Position" portion of the statement. The net liability is divided between the funds the City has set aside for future purposes and the gross amount of the City's debt that is intended to be funded in the future. The City has three funds:

The Operating Fund is primarily made up of the City's financial interest in its government business enterprises which consist of Toronto Hydro, Toronto Parking Authority, TEDCO and Enwave. It also includes the net financial interest in the City's agencies, boards and commissions (ABCs) of which the TTC, Toronto Community Housing Corporation (TCHC) and the Toronto Atmospheric Fund are the most prominent. The smallest portion of the fund represents the previous year's City surplus. The Capital Fund represents the net position of the City's capital projects. If the fund is in a deficit position, as it is in 2005, it indicates that the financing (such as a debt issuance) for these projects has yet to occur.

The reserves and reserve funds represent past revenues and contributions that have been set aside for future use. The majority of these funds are earmarked for future capital financing and for stabilizing the peaks and valleys of operating expenditures and revenue levels from year to year. A break down of the City's reserves and reserve funds can be found in Appendix 1 to the consolidated financial statements.

In addition to the reserves and reserve funds, the City also has received funds for specific purposes that have been deferred until related expenditures occur in the future. For example, developer charges and parkland dedication fees received are not recognized as revenues until such time as the projects for which the funds were raised are constructed. These funds are not included in the Municipal Position. A breakdown of the City's deferred revenues can be found in note 6 to the consolidated financial statements.

The Consolidated Statement of Financial Activities is sometimes considered to be the municipal equivalent to the private sector's income statement. However, like the Statement of Financial Position, there is an important distinction. Although the statements are on an accrual basis of accounting for most assets and liabilities, it is not "full" accrual accounting in that the cost of the City's physical assets are not amortized and depreciated over their useful life. Instead, the costs of the City's physical assets are expensed 100 per cent in the year they were purchased or built. PSAB is expected to announce later this year that all Canadian municipalities will be required to account for and report on their physical assets as of January 1, 2009.

The Consolidated Statement of Financial Activities provides a summary of the source, allocation and use of the City's financial resources throughout the reporting period. This statement reflects the combined operations of the operating, capital, reserve and reserve funds for the City and its consolidated entities.

The focus of this statement is the net expenditure/revenue figure found in the middle of the statement. A net expenditure figure represents an amount that the City has to finance from sources other than operating revenue. A net revenue figure represents an amount that the City could use to repay past financing or could set aside in reserves for future use. The financing section of the statement below this figure outlines the new long-term debt the City has issued (debentures) or assumed (employee benefits, property and liability claims, solid waste obligation) in the year and the debt retired in the year.

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ACCOUNTING CHANGES

The 2005 consolidated financial statements reflect a new PSAB standard for local governments relating to accounting and disclosure of liabilities and contingencies. Liabilities are now accounted for and reported when losses are considered likely and the amounts can be reasonably determined. The impact of this change is described in Note 2 to the Consolidated Financial Statements and relates to property and liability claims which were previously accounted for only upon the payment of a claim. The estimated liability for these claims is \$160 million as at December 31, 2005 .

2005 Highlights

- The City collected revenues of \$7.879 billion and spent \$8.111 billion for a net consolidated expenditure of \$232 million before long-term financing.
- As a result, the City's net financial liabilities increased from \$2.155 billion to \$2.388 billion.
- The level of unfinanced capital expenditure was decreased by \$120 million.
- Cash and investments increased by \$207 million to a total of \$2.645 billion.
- The City's investment in its government business enterprises decreased by \$23 million in 2005 to total \$1.013 billion.
- Net long-term debt to third parties increased by \$284 million to stand at \$1.965 billion at the end of the year.
- Mortgage debt obligations of Toronto Community Housing Corporation declined by \$27 million to a total of \$965 million at year end.
- The employee benefits liability increased by \$135 million to \$2.112 billion.

ANALYSIS

Current Operations – Budget to Actual Comparison

| Net revenues | 2005 (in thousands of dollars) | | |
|-----------------------|-----------------------------------|-----------|------------|
| | Budget | Actual | Difference |
| Property tax revenues | 3,151,673 | 3,235,363 | 83,690 |
| User charges | 1,791,199 | 1,766,557 | (24,642) |
| Government transfers | 1,654,052 | 1,591,894 | (62,158) |
| Other revenues | 684,604 | 693,175 | 8,571 |
| | 7,281,528 | 7,286,989 | 5,461 |
| Expenditures | 6,944,257 | 6,958,287 | 14,030 |
| Net revenues | 337,271 | 328,702 | (8,569) |

The favourable variance in property tax revenues is due to the City's more aggressive approach to ensure that new construction is assessed on a timely basis. As a result, additional resources applied by the Municipal Property Assessment Corporation in 2005 to assess built or renovated properties from 2004 and 2003 resulted in additional tax revenues of \$43 million. In addition, payments in lieu of taxes exceeded budget by \$43 million and relate to the fact that these revenues are budgeted on a net basis whereas payment in lieu revenues are recorded on a gross basis with write-offs reflected in general government expenditures. The unfavourable results in user charges relate to a \$22 million shortfall in the sale of water due to assumptions made with respect to consumption that did not materialize and a \$2 million reduction in paid waste tonnage at solid waste transfer stations. Government transfers were under budget by \$60 million due to reduced recoveries under cost shared programs in social assistance and social housing as a result of lower expenditures incurred in those programs.

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| Expenditures | 2005 <i>(in thousands of dollars)</i> | | |
|------------------------------------|--|------------------|-----------------|
| | Budget | Actual | Difference |
| General government | 570,029 | 550,613 | 19,416 |
| Protection to persons and property | 1,174,837 | 1,186,236 | (11,399) |
| Transportation | 1,415,058 | 1,417,252 | (2,194) |
| Environmental services | 549,461 | 555,938 | (6,477) |
| Health services | 301,565 | 315,260 | (13,695) |
| Social and family services | 1,642,433 | 1,596,895 | 45,538 |
| Social housing | 689,540 | 697,943 | (8,403) |
| Recreational and cultural services | 561,702 | 597,759 | (36,057) |
| Planning and development | 39,632 | 40,391 | (759) |
| Total | 6,944,257 | 6,958,287 | (14,030) |

The City budgets for employee benefits on a cash basis but reports these costs on an accrual basis in these consolidated financial statements. As a result, the 2005 Budget does not include \$135 million of employee benefit costs that have been incurred but are payable in future years whereas the actual expenditures reported in these consolidated financial statements, and reflected in all of the above expenditure categories, include these costs.

General government includes the expenditures of Council, internal support services and certain corporate programs such as property taxation. General government expenditures were under budget by \$19 million, due primarily to a \$30 million under expenditure in the allowance for property tax appeals as a result of the City becoming more active in the review of property assessments and participating in the tax appeal process for large properties. This was partially offset by unbudgeted property and liability claim expenditures of \$12 million as a result of the change in accounting for these liabilities during 2005 as noted earlier in this report.

Protection to persons and property includes the costs of Police, Fire, Building Services, Conservation Authority levies, and the Provincial Offences Act (POA) Courts. Actual costs in Fire were higher than budget due to an allocation of \$4 million in debenture debt costs in excess of budget.

Health Services expenditures were over budget due to higher than planned ambulance overtime costs related to patient offloading at hospitals and unbudgeted ambulance wage and benefit costs related to harmonization.

Social and family services expenditures were under budget due to a lower than budgeted number of caseloads, a lower than budgeted volume of services in Hostel Services and a delay in the construction of several large housing and shelter development projects.

Recreational and cultural services includes parks, recreation, cultural services, the Library Board and certain other City ABCs such as Exhibition Place, Toronto Zoo and Hummingbird Centre. Expenditures exceeded budget primarily due to overspending for hydro costs, salary expenditures and unanticipated storm damage costs in Parks, Forestry and Recreation.

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Adjustments to prior year's results

Included in the 2005 consolidated financial statements are two adjustments related to results in prior years. The impact of these adjustments are outlined in Note 18 to the consolidated financial statements.

The first item arises due to a spreadsheet error in the calculation of the present value of estimated future costs for post-closure costs in solid waste landfill liability estimates that was discovered this year and resulted in an increase of \$16 million in this liability as at December 31, 2004. The increase in this liability is offset by a similar increase in amounts to be recovered in future years as these liability estimates impact on tax levies that become necessary over the next 40 years. There is no net impact of this error on 2004 results as environmental services has been decreased by \$1 million and financing provided by changes in these obligations has been decreased by a similar amount.

The second item arises in the conversion of the accounts of Toronto Community Housing Corporation from a commercial basis of accounting to the PSAB basis which is followed in the preparation of these consolidated financial statements. In 2002, staff changed the consolidation procedure for TCHC but did not fully change the old procedures, resulting in the processing of an incorrect entry and the duplication of an elimination entry. These were identified in the 2005 consolidation process and the effect has been to reduce consolidated accounts receivable as at December 31, 2004 by \$24 million, to reduce the consolidated operating fund balance as at that date by a similar amount and to reduce consolidated other revenues reported for 2004 by \$25 million.

Comparison to the prior year

Net revenues for 2005 have increased when compared with 2004.

| Net revenues | <i>(in thousands of dollars)</i> | | |
|-----------------------|----------------------------------|------------------|----------------|
| | 2005 | 2004 | Difference |
| Property tax revenues | 3,235,363 | 3,096,416 | 138,947 |
| User charges | 1,766,557 | 1,681,994 | 84,563 |
| Government transfers | 1,591,894 | 1,527,933 | 63,961 |
| Other revenues | 693,175 | 599,450 | 93,725 |
| | 7,286,989 | 6,905,793 | 381,196 |
| Expenditures | 6,958,287 | 6,656,183 | 302,104 |
| Net revenues | 328,702 | 249,610 | 79,092 |

Property tax revenues increased in 2005 due to tax rate increases of 3 per cent and 1.5 per cent in the residential and commercial classes respectively, and an increase in supplementary taxes of \$43 million. Other revenues increased primarily because of a \$13 million increase in gross investment earnings, and \$12 million from the sale of land, \$14 million from a settlement with the Province upon the cancellation of certain housing projects, \$10 million from interest earned on sinking fund debentures and \$60 million in funds transferred from obligatory reserve funds.

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| Expenditures | <i>(in thousands of dollars)</i> | | |
|------------------------------------|----------------------------------|------------------|----------------|
| | 2005 | 2004 | Difference |
| General government | 550,613 | 546,505 | 4,108 |
| Protection to persons and property | 1,186,236 | 1,232,623 | (46,387) |
| Transportation | 1,417,252 | 1,340,054 | 77,198 |
| Environmental services | 555,938 | 536,389 | 19,549 |
| Health services | 315,260 | 302,864 | 12,396 |
| Social and family services | 1,596,895 | 1,488,463 | 108,432 |
| Social housing | 697,943 | 628,977 | 68,966 |
| Recreational and cultural services | 597,759 | 544,099 | 53,660 |
| Planning and development | 40,391 | 36,209 | 4,182 |
| Total | 6,958,287 | 6,656,183 | 302,104 |

Capital Operations

Budget to Actual Comparison

| Net Expenditures | <i>(in thousands of dollars)</i> | | |
|-------------------------------------|----------------------------------|------------------|----------------|
| | 2005 Budget | 2005 Actual | 2004 Actual |
| Expenditures | 1,681,565 | 1,152,818 | 1,122,462 |
| Revenues | 705,753 | 522,392 | 404,920 |
| Debentures | 615,906 | 500,000 | 375,000 |
| Operating fund transfers | 197,308 | 197,248 | 163,402 |
| Net reserve/reserve fund transfers | 131,757 | 42,405 | 35,197 |
| Landfill obligations | - | 10,434 | 3,568 |
| Total revenues and financing | 1,650,724 | 1,272,479 | 982,087 |
| Net expenditures (financing) | 30,841 | (119,661) | 140,375 |

Capital expenditure levels continue to be well under budget. The principle reason for the under expenditure were delays encountered due to scheduling requirements and the need to integrate construction schedules of several capital projects.

Current Accounts

Note 3 to the consolidated financial statements provides details about the City's investment portfolios and their yields. Note 4 provides additional information on the City's note receivable from Toronto Hydro. Information about the City's government business enterprises is found in note 5 and Appendix 2 to the consolidated financial statements.

Taxes Receivable

Taxes receivable includes all outstanding taxes, items that have been added to the tax roll such as utilities arrears, drainage charges, local improvement charges, accumulated penalties and interest charges against such taxes, less any allowance for uncollectable taxes. A breakdown of this receivable is noted on the following page:

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| Taxes Receivable | <i>(in millions of dollars)</i> | |
|---------------------------------------|---------------------------------|--------------|
| | 2005 | 2004 |
| Current year | 191.9 | 154.5 |
| Prior year | 34.7 | 25.7 |
| Previous years | 21.9 | 39.6 |
| Interest/penalty | 29.4 | 29.5 |
| Less: allowance for doubtful accounts | (11.2) | (23.3) |
| Net receivables | 266.7 | 226.0 |

The increase in current year taxes relates primarily to supplementary tax levies billed late in the year for \$20 million and the automated transfer to the Collector's Roll during 2005 of overdue water accounts of which \$12 million was outstanding at year-end.

Accounts Payable

The breakdown of accounts payable and accrued liabilities at December 31, 2005 with 2004 comparatives is as follows:

| Accounts Payable | <i>(in millions of dollars)</i> | |
|--|---------------------------------|----------------|
| | 2005 | 2004 |
| Local Board trade payables | 331.9 | 306.8 |
| City trade payables and accruals | 744.1 | 775.0 |
| Payable to school boards | 262.5 | 291.7 |
| Provision for assessment appeals | 314.5 | 263.9 |
| Credit balances on property tax accounts | 66.4 | 75.2 |
| Payroll liabilities | 81.6 | 68.2 |
| Total | 1,801.0 | 1,780.8 |

Accounts Receivable

The breakdown of accounts receivable and accrued amounts owed to the City at December 31, 2005 with 2004 comparatives is as follows:

| Accounts Receivable | <i>(in thousands of dollars)</i> | |
|-----------------------------|----------------------------------|----------------|
| | 2005 | 2004 |
| Government of Canada | 120,789 | 17,061 |
| Government of Ontario | 30,325 | 839 |
| Other municipal governments | 978 | 1,288 |
| School board | 1,345 | 3,778 |
| Water fees | 88,229 | 103,669 |
| Other | 471,883 | 489,231 |
| Total | 713,469 | 615,866 |

The increases in amounts due from the federal and provincial governments are attributed to new funding available for infrastructure and transit expenditures pursuant to the gas tax agreements with the federal and provincial governments of \$98 million and \$30 million respectively.

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Significant Trends

Significant trend information is provided below for key financial indicators over the last five years.

Financial Activities

Capital and Operating

(in thousands of dollars)

| Consolidated Net Expenditures | Avg. Annual Increase | 2005 | 2004 | 2003 | 2002 | 2001 |
|-------------------------------|----------------------|-----------|-----------|-----------|-----------|-----------|
| Revenues | 3.98% | 7,879,032 | 7,354,486 | 7,230,705 | 7,084,372 | 6,745,486 |
| Expenditures | 4.33% | 8,111,105 | 7,778,645 | 7,360,506 | 7,081,194 | 6,845,850 |
| Net (expenditures) revenues | A | (232,073) | (424,159) | (129,801) | 3,178 | (100,364) |

(in thousands of dollars)

| Financing | | 2005 | 2004 | 2003 | 2002 | 2001 |
|---|-------|---------|---------|---------|---------|----------|
| Net new debentures and mortgages net of repayment | | 271,936 | 198,003 | 138,826 | 3,670 | 72,692 |
| Increase in unfunded liabilities | | 156,989 | 217,929 | 131,612 | 135,182 | 170,633 |
| Increase (decrease) in inventories and prepaid expenses | | 1,107 | 1,536 | 18,483 | (6,454) | (14,048) |
| Total financing and inventory change | B | 430,032 | 417,468 | 288,921 | 132,398 | 229,277 |
| Increase (decrease) in Fund balances | (A+B) | 197,959 | (6,691) | 159,120 | 135,576 | 128,913 |

The trend of expenditure levels exceeding revenues continued in 2005 and has been financed with the issuance of increasingly higher levels of debenture debt (\$272 million total net) and increases in unfunded liabilities (\$157.0 million). The increase in unfunded liabilities, while not requiring cash funding in the current year, will require higher tax levies in future years in the absence of the realization of other sources of revenue.

Revenues

The table below demonstrates that property taxes continue to be the slowest growing revenue source for the City. During this period, assessment growth has been minimal. Gains made by new construction have been offset by conversions of non-residential classes to residential classes (which is taxed at a much lower rate) and by property tax appeals on current value assessments. In addition, the City has been limited by provincial legislation from extending tax rate increases on the commercial, industrial and multi-residential assessment base to 50 per cent of the tax rate increase applied to residential assessment. The commercial, industrial and multi-residential assessment base represents approximately 61 per cent of the City's tax revenue base. As a result more reliance has been placed on user fees, government grants and other sources of revenue to meet expenditures.

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(in thousands of dollars)

| Consolidated Revenues | Avg. Annual Increase | 2005 | 2004 | 2003 | 2002 | 2001 |
|-----------------------------|----------------------|------------------|------------------|------------------|------------------|------------------|
| Property taxes | 2.18% | 3,235,363 | 3,096,416 | 2,983,563 | 2,968,475 | 2,970,485 |
| User charges | 3.76% | 1,766,557 | 1,681,994 | 1,635,996 | 1,625,970 | 1,525,665 |
| Senior government transfers | 7.10% | 1,831,399 | 1,600,688 | 1,636,202 | 1,576,589 | 1,403,198 |
| Other | 5.49% | 1,045,713 | 975,388 | 974,944 | 913,338 | 846,138 |
| Total | 3.98% | 7,879,032 | 7,354,486 | 7,230,705 | 7,084,372 | 6,745,486 |

Included in other revenues are earnings from government business enterprises, investment income, revenues from the sale of land and contributions from deferred revenue.

*Financial Position**(in thousands of dollars)*

| Net Liabilities | 2005 | 2004 | 2003 | 2002 | 2001 |
|--|------------------|------------------|------------------|------------------|------------------|
| Liabilities | 8,067,913 | 7,526,205 | 6,615,416 | 6,431,411 | 6,236,701 |
| Financial Assets, inventories and prepaid expenses | 5,825,636 | 5,514,894 | 5,163,189 | 5,052,657 | 4,861,223 |
| Net Liabilities | 2,242,277 | 2,011,311 | 1,452,227 | 1,378,754 | 1,375,478 |

As mentioned earlier in this report, the City's physical or "fixed" assets, including land, buildings, equipment and infrastructure, are not disclosed in these financial statements but needs to be considered in any review of the City's financial position. The City's net liabilities have increased by an average annual rate of 11.0 per cent over the last five years and is attributable to increases in long-term debt to third parties and in employee benefit liabilities. The following table illustrates this:

(in thousands of dollars)

| Long-Term Debt | Avg. Annual Increase | 2005 | 2004 | 2003 | 2002 | 2001 |
|------------------------------|----------------------|------------------|------------------|------------------|------------------|------------------|
| Third Party Debt: | | | | | | |
| Debentures | 11.54% | 1,794,950 | 1,505,361 | 1,301,457 | 1,158,827 | 1,171,388 |
| Provincial loan | (1.88%) | 170,171 | 175,331 | 175,331 | 183,750 | 183,750 |
| TCHC Mortgages | (1.88%) | 965,396 | 992,571 | 1,017,078 | 1,035,843 | 1,041,603 |
| | 5.23% | 2,930,517 | 2,673,263 | 2,493,866 | 2,378,420 | 2,396,741 |
| Employee Benefit Liabilities | 8.07% | 2,112,288 | 1,977,775 | 1,791,750 | 1,654,495 | 1,549,119 |
| Total | 6.36% | 5,042,805 | 4,651,038 | 4,285,616 | 4,032,915 | 3,945,860 |

Additional information on the mortgage obligations of Toronto Community Housing Corporation can be found in Note 8 in the consolidated financial statements. Note 9 in the consolidated financial statements provides additional information about the provincial loan and the City's debenture debt. Further details about the City's employee benefits liabilities can be found in Note 10 to the consolidated financial statements.

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(in thousands of dollars)

| Reserves and Reserve Funds | 2005 | 2004 | 2003 | 2002 | 2001 |
|----------------------------|----------------|----------------|----------------|----------------|----------------|
| Reserves | 196,485 | 178,801 | 269,685 | 319,558 | 238,906 |
| Reserve Funds | 694,412 | 700,128 | 663,478 | 571,834 | 442,118 |
| Total | 890,897 | 878,929 | 933,163 | 891,392 | 681,024 |

The City's reserves and reserve funds generally represent "stabilization" reserves that are used to smooth expenditure and revenue variances from one year to the next and "capital" reserves that are used to fund a portion of the City's capital program. Appendix 1 to the financial statements provides a breakdown of the City's reserves and reserve funds.

Summary

The City's net financial liabilities increased in 2005 largely due to increases in long-term debt and unfunded employee benefit liabilities. In absence of new revenue sources, the City will need to rely increasingly on debt to finance its capital program and to implement significant property tax increases to finance the operating program. While some progress has been made in securing additional revenue sharing arrangements with the federal and provincial governments, the City still requires new revenue streams that grow with the economy so that fiscal sustainability can be achieved.

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2005 CONSOLIDATED FINANCIAL STATEMENTS

The audited numbers for vigilance in
fiscal prudence



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AUDITED FINANCIAL STATEMENTS

MANAGEMENT'S REPORT

The management of the City of Toronto is responsible for the integrity, objectivity and accuracy of the financial information presented in the accompanying consolidated financial statements.

The consolidated financial statements have been prepared by management in accordance with generally accepted accounting principles established by the Canadian Institute of Chartered Accountants' Public Sector Accounting Board. A summary of the significant accounting policies is disclosed in Note 1 to the financial statements.

To meet its responsibility, management maintains comprehensive financial and internal control systems designed to ensure the proper authorization of transactions, the safeguarding of assets and the integrity of the financial data. The City employs highly qualified professional staff and deploys an organizational structure that effectively segregates responsibilities, and appropriately delegates authority and accountability.

The Audit Committee, a sub committee of City Council, reviews and approves the financial statements before they are submitted to Council. In accordance with Council's directive, the Auditor General oversees the work of the external auditors performing financial statement attest audits. While it is important to recognize that the external audit is an independent process, the Auditor General's role is to ensure that all significant audit issues are appropriately addressed and resolved. In this context, the Auditor General participates in all significant meetings held between the external auditors and management.

The 2005 consolidated financial statements have been examined by the City of Toronto's external auditors, Ernst & Young LLP, Chartered Accountants, and their report precedes the financial statements.

Toronto, Canada
April 28, 2006

Cam Weldon
Treasurer

Joseph P. Pennachetti
Deputy City Manager & Chief Financial Officer

Shirley Hoy
City Manager

AUDITORS' REPORT

To the Members of Council, Inhabitants and Ratepayers of the City of Toronto

We have audited the consolidated statement of financial position of the City of Toronto as at December 31, 2005 and the consolidated statements of financial activities and cash flows for the year then ended. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the City as at December 31, 2005 and the results of its financial activities and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Toronto, Canada
May 5, 2006.

Ernst + Young LLP

Chartered Accountants

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at December 31, 2005

(with comparative figures as at December 31, 2004)

| | 2005 | 2004 |
|---|--------------------|---|
| | (\$000) | (\$000) (Restated) (Notes 2 and 18) |
| FINANCIAL ASSETS | | |
| Cash | 54,753 | 65,187 |
| Accounts receivable | 713,469 | 615,866 |
| Property taxes receivable | 266,735 | 225,963 |
| Other assets | 4,397 | 2,839 |
| Investments (Note 3) | 2,590,043 | 2,372,396 |
| Note receivable – Toronto Hydro Corporation (Note 4) | 980,231 | 980,231 |
| Receivable from Toronto District School Board (Note 9) | 58,021 | 72,703 |
| Investments in government business enterprises (Note 5) | 1,012,568 | 1,035,397 |
| Total Financial Assets | 5,680,217 | 5,370,582 |
| FINANCIAL LIABILITIES | | |
| Accounts payable and accrued liabilities | 1,800,992 | 1,780,751 |
| Deferred revenue (Note 6) | 882,968 | 783,328 |
| Other liabilities (Notes 2 and 16) | 216,123 | 196,497 |
| Landfill closure and post-closure liabilities (Note 7) | 125,025 | 114,591 |
| Mortgages payable (Note 8) | 965,396 | 992,571 |
| Net long-term debt (Note 9) | 1,965,121 | 1,680,692 |
| Employee benefit liabilities (Note 10) | 2,112,288 | 1,977,775 |
| Total Financial Liabilities | 8,067,913 | 7,526,205 |
| NET FINANCIAL LIABILITIES | (2,387,696) | (2,155,623) |
| NON-FINANCIAL ASSETS | | |
| Inventories and prepaid expenses | 145,419 | 144,312 |
| NET LIABILITIES | (2,242,277) | (2,011,311) |
| MUNICIPAL POSITION | | |
| FUND BALANCES | | |
| Operating fund (Schedule 1) | 2,381,862 | 2,315,532 |
| Capital fund (Note 12 and Schedule 2) | (245,159) | (364,820) |
| Reserves and reserve funds (Schedule 3) | 890,897 | 878,929 |
| TOTAL FUND BALANCES | 3,027,600 | 2,829,641 |
| Amounts to be recovered in future years: | | |
| From reserves and reserve funds on hand | (283,287) | (294,386) |
| From future revenues | (4,986,590) | (4,546,566) |
| TOTAL AMOUNTS TO BE RECOVERED (Note 11) | (5,269,877) | (4,840,952) |
| TOTAL MUNICIPAL POSITION | (2,242,277) | (2,011,311) |

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

CONSOLIDATED STATEMENT OF FINANCIAL ACTIVITIES

For the year ended December 31, 2005
(with comparative figures for the year ended December 31, 2004)

| | 2005 BUDGET (\$'000) (Note 15) | 2005 ACTUALS (\$'000) | 2004 ACTUALS (\$'000) (Restated) (Notes 2 and 18) |
|---|---|-----------------------------|---|
| REVENUES | | | |
| Residential and commercial property taxation | 3,067,743 | 3,122,120 | 3,016,817 |
| Taxation from other governments | 83,930 | 113,243 | 79,599 |
| User charges | 1,791,199 | 1,766,557 | 1,681,994 |
| Funding transfers from other governments | 1,796,780 | 1,831,399 | 1,600,688 |
| Net government business enterprise earnings (Note 5) | - | 102,376 | 112,215 |
| Other | 1,312,102 | 943,337 | 863,173 |
| TOTAL REVENUES | 8,051,754 | 7,879,032 | 7,354,486 |
| EXPENDITURES | | | |
| General government | 695,293 | 612,754 | 602,039 |
| Protection to persons and property | 1,276,543 | 1,253,880 | 1,287,582 |
| Transportation | 2,131,692 | 1,963,608 | 1,888,948 |
| Environmental services | 943,094 | 781,706 | 755,952 |
| Health services | 314,675 | 324,191 | 310,547 |
| Social and family services | 1,677,569 | 1,610,249 | 1,520,593 |
| Social housing | 797,420 | 797,505 | 722,452 |
| Recreation and cultural services | 688,070 | 691,791 | 632,941 |
| Planning and development | 101,466 | 75,421 | 57,591 |
| TOTAL EXPENDITURES (Note 13) | 8,625,822 | 8,111,105 | 7,778,645 |
| NET EXPENDITURES AND INCREASE IN NET FINANCIAL LIABILITIES | (574,068) | (232,073) | (424,159) |
| FINANCING | | | |
| New long-term debt and mortgages issued | 615,906 | 500,000 | 375,000 |
| Principal repayments on long-term debt and mortgages | (178,631) | (198,451) | (154,952) |
| Interest earned on sinking funds | - | (29,613) | (22,045) |
| Changes in solid waste landfill obligations | - | 10,434 | 3,568 |
| Changes in property and liability claims | - | 12,042 | 28,336 |
| Changes in employee benefit liabilities | - | 134,513 | 186,025 |
| NET INCREASE IN AMOUNTS TO BE RECOVERED IN FUTURE YEARS | 437,275 | 428,925 | 415,932 |
| INCREASE IN NON-FINANCIAL ASSETS | - | 1,107 | 1,536 |
| INCREASE (DECREASE) IN FUND BALANCES | (136,793) | 197,959 | (6,691) |
| FUND BALANCES - BEGINNING OF YEAR | 909,770 | 2,829,641 | 2,836,332 |
| FUND BALANCES - END OF YEAR | 772,977 | 3,027,600 | 2,829,641 |

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

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended December 31, 2005

(with comparative figures for the year ended December 31, 2004)

| | 2005 (\$000) | 2004 (\$000) (Restated) (Notes 2 and 18) |
|---|-----------------|---|
| OPERATIONS | | |
| Net expenditures for the year | (232,073) | (424,159) |
| Uses of cash: | | |
| Increase in accounts receivable | (97,603) | (100,026) |
| Increase in property taxes receivable | (40,772) | - |
| Increase in other assets | (1,558) | - |
| Decrease in other liabilities | - | (35,003) |
| | (139,933) | (135,029) |
| Sources of cash: | | |
| Decrease in other assets | - | 2,588 |
| Decrease in property taxes receivable | - | 21,026 |
| Increase in accounts payable accrued liabilities | 20,241 | 200,088 |
| Increase in deferred revenue | 99,640 | 239,439 |
| Increase in other liabilities | 19,626 | - |
| Increase in landfill closure and post-closure liabilities | 10,434 | 3,568 |
| Increase in employee benefit liabilities | 134,513 | 186,025 |
| | 284,454 | 652,734 |
| Net increase (decrease) in cash from operations | (87,552) | 93,546 |
| INVESTING | | |
| Net increase in investments | (217,647) | (234,441) |
| Net decrease (increase) in investments in government business enterprises | 22,829 | (75,994) |
| Net decrease in receivable from Toronto District School Board | 14,682 | 18,606 |
| Net decrease in cash from investing | (180,136) | (291,829) |
| FINANCING | | |
| New long-term debt and mortgages issued | 500,000 | 375,000 |
| Principal repayments on long-term debt and mortgages | (198,451) | (154,952) |
| Interest earned on sinking funds | (29,613) | (22,045) |
| Principal repayments on debt by Toronto District School Board | (14,682) | (18,606) |
| Net increase in cash from financing | 257,254 | 179,397 |
| NET DECREASE – CASH | (10,434) | (18,886) |
| CASH – BEGINNING OF YEAR | 65,187 | 84,073 |
| CASH – END OF YEAR | 54,753 | 65,187 |

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

ANALYSIS OF CONSOLIDATED CURRENT OPERATIONS - SCHEDULE 1

For the year ended December 31, 2005

(with comparative figures for the year ended December 31, 2004)

| | 2005 BUDGET (\$'000) | 2005 ACTUALS (\$'000) | 2004 ACTUALS (\$'000) (Restated) (Notes 2 and 18) |
|---|----------------------------|-----------------------------|---|
| EXPENDITURES | | | |
| General government | | | |
| Council | 17,881 | 17,254 | 17,348 |
| Administration | 428,339 | 441,289 | 404,728 |
| Ontario property assessment | 31,200 | 29,881 | 29,004 |
| Allowance for property tax appeals | 92,609 | 62,189 | 95,425 |
| | 570,029 | 550,613 | 546,505 |
| Protection to persons and property | | | |
| Fire | 309,794 | 325,066 | 347,522 |
| Police | 749,000 | 743,926 | 774,841 |
| Building services | 80,045 | 81,666 | 76,363 |
| Other | 35,998 | 35,578 | 33,897 |
| | 1,174,837 | 1,186,236 | 1,232,623 |
| Transportation | | | |
| Transit | 1,068,088 | 1,074,846 | 1,011,631 |
| Road/traffic signals maintenance | 346,970 | 342,406 | 328,423 |
| | 1,415,058 | 1,417,252 | 1,340,054 |
| Environmental services | | | |
| Water | 157,450 | 164,174 | 163,984 |
| Wastewater | 180,701 | 180,756 | 174,116 |
| Solid waste | 211,310 | 211,008 | 198,289 |
| | 549,461 | 555,938 | 536,389 |
| Health services | | | |
| Ambulance | 126,853 | 140,283 | 139,229 |
| Public health services | 174,712 | 174,977 | 163,635 |
| | 301,565 | 315,260 | 302,864 |
| Social and family services | | | |
| Social assistance | 1,160,614 | 1,118,964 | 1,045,260 |
| Long-term care | 181,154 | 182,627 | 169,507 |
| Child care assistance | 300,665 | 295,304 | 273,696 |
| | 1,642,433 | 1,596,895 | 1,488,463 |
| Social housing | | | |
| | 689,540 | 697,943 | 628,977 |
| Recreation and cultural services | | | |
| Parks | 107,550 | 122,831 | 107,788 |
| Recreation | 211,613 | 230,380 | 187,729 |
| Other | 242,539 | 244,548 | 248,582 |
| | 561,702 | 597,759 | 544,099 |
| Planning and development | | | |
| Planning | 29,685 | 28,733 | 25,389 |
| Business development | 9,947 | 11,658 | 10,820 |
| | 39,632 | 40,391 | 36,209 |
| Total Expenditures | 6,944,257 | 6,958,287 | 6,656,183 |

ANALYSIS OF CONSOLIDATED CURRENT OPERATIONS - SCHEDULE 1

For the year ended December 31, 2005

(with comparative figures for the year ended December 31, 2004)

| | 2005 BUDGET (\$'000) | 2005 ACTUALS (\$'000) | 2004 ACTUALS (\$'000) (Restated) (Notes 2 and 18) |
|--|----------------------------|-----------------------------|---|
| REVENUES | | | |
| Residential and commercial property taxation | 3,067,743 | 3,122,120 | 3,016,817 |
| Taxation from other governments | 83,930 | 113,243 | 79,599 |
| User charges: | | | |
| Transit fares | 705,300 | 714,509 | 685,425 |
| Water sales | 561,427 | 541,132 | 476,101 |
| Fines | 120,879 | 130,991 | 133,126 |
| Licenses and permits | 100,186 | 94,955 | 92,750 |
| Fees and service charges | 303,407 | 284,970 | 294,592 |
| Government transfers: | | | |
| Social assistance | 694,520 | 650,208 | 623,899 |
| Child care assistance | 209,667 | 203,273 | 185,659 |
| Health services | 106,658 | 104,954 | 89,957 |
| Social housing | 388,988 | 365,436 | 354,844 |
| Other | 254,219 | 268,023 | 273,574 |
| Investment income | 226,119 | 138,863 | 125,437 |
| Net government business enterprises earnings (Note 5) | - | 102,376 | 112,215 |
| Other | 458,485 | 451,936 | 361,798 |
| Total Revenues | 7,281,528 | 7,286,989 | 6,905,793 |
| NET REVENUES FOR THE YEAR | 337,271 | 328,702 | 249,610 |
| FINANCING AND TRANSFERS | | | |
| Principal repayments on long-term debt and mortgages | (178,631) | (198,451) | (154,952) |
| Interest earned on sinking funds | - | (29,613) | (22,045) |
| Changes in employee benefit liabilities | - | 134,513 | 186,025 |
| Changes in property and liability claims | - | 12,042 | 28,336 |
| Transfers from (to) reserves | (33,962) | (50,477) | 44,997 |
| Transfers from reserve funds | 72,630 | 65,755 | 17,813 |
| Transfers to capital fund | (197,308) | (197,248) | (163,402) |
| Total Financing and Transfers | (337,271) | (243,479) | (63,228) |
| Increase in Non-Financial Assets | - | 1,107 | 1,536 |
| NET INCREASE IN OPERATING FUND BALANCE FOR THE YEAR | - | 66,330 | 187,918 |
| OPERATING FUND BALANCE - BEGINNING OF YEAR | - | 2,315,532 | 2,127,614 |
| OPERATING FUND BALANCE - END OF YEAR | - | 2,381,862 | 2,315,532 |

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

ANALYSIS OF CONSOLIDATED CAPITAL OPERATIONS - SCHEDULE 2

For the year ended December 31, 2005
(with comparative figures for the year ended December 31, 2004)

| | 2005 BUDGET (\$'000) | 2005 ACTUALS (\$'000) | 2004 ACTUALS (\$'000) (Restated) (Note 18) |
|---|----------------------------|-----------------------------|--|
| EXPENDITURES | | | |
| General government | 125,264 | 62,141 | 55,534 |
| Protection to persons and property | | | |
| Fire 28,152 | 13,829 | 10,497 | |
| Police | 65,219 | 45,628 | 32,628 |
| Other | 8,335 | 8,187 | 11,834 |
| | 101,706 | 67,644 | 54,959 |
| Transportation | | | |
| Transit | 405,042 | 389,481 | 324,301 |
| Roads | 311,592 | 156,875 | 224,593 |
| | 716,634 | 546,356 | 548,894 |
| Environmental services | | | |
| Water | 204,945 | 112,641 | 112,808 |
| Wastewater | 144,119 | 73,739 | 61,300 |
| Solid waste | 44,569 | 39,388 | 45,455 |
| | 393,633 | 225,768 | 219,563 |
| Health services | | | |
| Ambulance | 11,597 | 8,141 | 6,920 |
| Public health services | 1,513 | 790 | 763 |
| | 13,110 | 8,931 | 7,683 |
| Social and family services | | | |
| Social assistance | 10,426 | 5,531 | 14,552 |
| Long-term care | 11,734 | 5,172 | 12,240 |
| Child care assistance | 12,976 | 2,651 | 5,338 |
| | 35,136 | 13,354 | 32,130 |
| Social housing | 107,880 | 99,562 | 93,475 |
| Recreation and cultural services | | | |
| Parks | 46,397 | 22,736 | 20,094 |
| Recreation | 48,711 | 26,770 | 29,405 |
| Other | 31,260 | 44,526 | 39,343 |
| | 126,368 | 94,032 | 88,842 |
| Planning and development | | | |
| Planning | 8,663 | 3,050 | 4,290 |
| Business development | 53,171 | 31,980 | 17,092 |
| | 61,834 | 35,030 | 21,382 |
| Total Expenditures | 1,681,565 | 1,152,818 | 1,122,462 |

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

ANALYSIS OF CONSOLIDATED CAPITAL OPERATIONS - SCHEDULE 2

For the year ended December 31, 2005

(with comparative figures for the year ended December 31, 2004)

| | 2005 BUDGET (\$'000) | 2005 ACTUALS (\$'000) | 2004 ACTUALS (\$'000) (Restated) (Note 18) |
|---|----------------------------|-----------------------------|--|
| REVENUES | | | |
| Government of Canada transfers | 54,591 | 164,427 | 12,661 |
| Province of Ontario transfers | 88,137 | 75,078 | 60,094 |
| Other municipalities | 17,503 | 4,843 | 1,236 |
| Other | 545,522 | 278,044 | 330,929 |
| Total Revenues | 705,753 | 522,392 | 404,920 |
| NET EXPENDITURES FOR THE YEAR | (975,812) | (630,426) | (717,542) |
| FINANCING AND TRANSFERS | | | |
| New long-term debt and mortgages issued | 615,906 | 500,000 | 375,000 |
| Changes in solid waste landfill obligations (Note 7) | - | 10,434 | 3,568 |
| Transfers from operating fund | 197,308 | 197,248 | 163,402 |
| Transfers from reserves | 82,629 | 32,793 | 15,822 |
| Transfers from reserve funds | 49,128 | 9,612 | 19,375 |
| Total Financing and Transfers | 944,971 | 750,087 | 577,167 |
| NET INCREASE (DECREASE) IN CAPITAL FUND BALANCE FOR THE YEAR | (30,841) | 119,661 | (140,375) |
| CAPITAL FUND BALANCE – BEGINNING OF YEAR | 30,841 | (364,820) | (224,445) |
| CAPITAL FUND BALANCE – END OF YEAR | - | (245,159) | (364,820) |

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

ANALYSIS OF CONSOLIDATED RESERVES AND CONSOLIDATED RESERVE FUNDS - SCHEDULE 3

For the year ended December 31, 2005

(with comparative figures for the year ended December 31, 2004)

| | 2005 BUDGET (\$'000) | 2005 ACTUALS (\$'000) | 2004 ACTUALS (\$'000) |
|--|----------------------------|-----------------------------|-----------------------------|
| RESERVES | | | |
| TRANSFERS FROM (TO) OTHER FUNDS | | | |
| Reserve fund | - | - | (30,065) |
| Operating fund | 33,962 | 50,477 | (44,997) |
| Capital fund | (82,629) | (32,793) | (15,822) |
| NET TRANSFERS FROM (TO) OTHER FUNDS FOR THE YEAR | (48,667) | 17,684 | (90,884) |
| RESERVES BALANCE - BEGINNING OF YEAR | 178,801 | 178,801 | 269,685 |
| RESERVES BALANCE - END OF YEAR | 130,134 | 196,485 | 178,801 |
| RESERVE FUNDS | | | |
| REVENUES | | | |
| Sale of land | 27,761 | 17,713 | 6,570 |
| Investment income | 36,712 | 34,111 | 31,658 |
| Other | - | 17,827 | 5,545 |
| TOTAL REVENUES | 64,473 | 69,651 | 43,773 |
| TRANSFERS FROM (TO) OTHER FUNDS | | | |
| Reserves | - | - | 30,065 |
| Operating fund | (72,630) | (65,755) | (17,813) |
| Capital fund | (49,128) | (9,612) | (19,375) |
| NET TRANSFERS TO OTHER FUNDS | (121,758) | (75,367) | (7,123) |
| NET INCREASE (DECREASE) IN RESERVE FUNDS BALANCE FOR THE YEAR | (57,285) | (5,716) | 36,650 |
| RESERVE FUNDS BALANCE - BEGINNING OF YEAR | 700,128 | 700,128 | 663,478 |
| RESERVE FUNDS BALANCE - END OF YEAR | 642,843 | 694,412 | 700,128 |
| TOTAL RESERVES AND RESERVE FUNDS | 772,977 | 890,897 | 878,929 |

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

1. Significant Accounting Policies

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles established by the Public Sector Accounting Board ("PSAB") of the Canadian Institute of Chartered Accountants.

Basis of Consolidation

The consolidated financial statements reflect the assets, liabilities, revenues and expenditures of the operating fund, capital fund, reserves and reserve funds of the City of Toronto (the "City") and, except for government business enterprises which are accounted for by the modified equity basis of accounting, include all organizations that are accountable for the administration of their financial affairs and resources to City Council ("Council") and are controlled by the City.

Consolidated entities:

Agencies, Boards and Commissions

- Exhibition Place
- Heritage Toronto
- Hummingbird Centre for the Performing Arts
- North York Performing Arts Centre Corporation
- St. Lawrence Centre for the Arts
- Toronto Atmospheric Fund
- Toronto Board of Health
- Toronto Community Housing Corporation
- Toronto Licensing Commission
- Toronto Police Services Board
- Toronto Public Library Board
- Toronto Transit Commission
- Toronto Zoo
- Yonge-Dundas Square

Arenas:

- Forest Hill Memorial
- George Bell
- Leaside Memorial Community Gardens
- McCormick Playground
- Moss Park
- North Toronto Memorial
- Ted Reeve
- William H. Bolton

Community Centres:

- 519 Church Street
- Applegrove
- Cecil Street
- Central Eglinton
- Community Centre 55
- Eastview Neighbourhood
- Harbourfront
- Ralph Thornton
- Scadding Court
- Swansea Town Hall

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

Business Improvement Areas:

- Beaches Bloor Annex
- Bloor by the Park
- Bloorcourt Village
- Bloordale Village
- Bloor West Village
- Bloor-Yorkville
- Church-Wellesley
- College Promenade
- Corso Italia
- The Danforth
- Dovercourt Village
- Downtown Yonge
- Eglinton Hill
- Eglinton Way
- Emery Village
- Forest Hill Village
- Gerrard India Bazaar
- Greektown on the Danforth
- Harbord Street
- Hillcrest Village
- Junction Gardens
- Kennedy Road
- Kingsway
- Knob Hill Plaza
- Korea Town
- Lakeshore Village
- Liberty Village
- Little Italy
- Long Branch
- Mimico by the Lake
- Mimico Village
- Mirvish Village
- Mount Dennis
- Old Cabbagetown
- Parkdale Village
- Pape Village
- Queens Quay Harbour-Front
- Riverside
- Roncesvalles Village
- Rosedale Main Street
- St. Clair Gardens
- St. Clair Avenue West
- St. Lawrence Neighbourhood
- Upper Village (Toronto)
- Upper Village (York)
- Village of Islington
- Weston
- West Queen West
- Wexford
- Wexford Wychwood Heights
- Yonge-Lawrence Village
- York-Eglinton

All interfund assets and liabilities and sources of financing and expenditures have been eliminated in these consolidated financial statements.

Government Business Enterprises

The following entities are accounted for in these consolidated financial statements as government business enterprises using the modified equity basis of accounting. Under the modified equity basis, the accounting principles of government business enterprises are not adjusted to conform to the City's accounting principles and inter-organizational transactions and balances are not eliminated, inter-organizational gains and losses are however eliminated on assets remaining within the government reporting entities at the reporting date.

- Enwave District Energy Limited ("Enwave")
- Toronto Economic Development Corporation ("TEDCO")
- Toronto Hydro Corporation
- Toronto Parking Authority

Trust Funds

Trust funds and their related operations administered by the City are not included in the consolidated financial statements, but are reported separately on the Trust Fund Statement of Continuity and the Trust Fund Balance Sheet (Note 14).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

Basis of Accounting

Revenues and expenditures are reported on the accrual basis of accounting. The accrual basis of accounting recognizes revenues as they are earned and measurable; expenditures are recognized as they are incurred and measurable as a result of the receipt of goods or services and the creation of a legal obligation to pay.

Capital Assets

The historical cost and accumulated depreciation of capital assets are not reported. Capital assets are reported as an expenditure on the Consolidated Statement of Financial Activities in the year of acquisition.

Use of Estimates

The preparation of these consolidated financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions which affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures for the year. These estimates and assumptions, including such areas as employee benefits, assessment appeals, claims provisions, landfill liabilities and environmental provisions, are based on the City's best information and judgement and may differ significantly based on actual results.

Investments

Investments are recorded at amortized cost less any amounts written off to reflect a permanent decline in value. Investments consist of authorized investments pursuant to provisions of the Municipal Act and comprise government and corporate bonds, debentures and short-term instruments of various financial institutions.

Property and Liability Claims

Estimated costs to settle claims are based on available loss information and projections of estimated future expenditures developed from the City's historical experience on loss payments. Claims are reported as an operating expenditure in the year of the loss, where the costs are deemed to be likely and can be reasonably determined, and are reported as a liability on the Consolidated Statement of Financial Position.

Environmental Provisions

The City provides for the cost of compliance with environmental legislation when conditions are identified which indicate non-compliance with environmental legislation and costs can be reasonably determined. The estimated amounts of future restoration costs are reviewed regularly, based on available information and governing legislation.

Landfill Closure and Post-Closure Liabilities

The estimated costs to maintain closed solid waste landfill sites are based on estimated future expenditures in current dollars, adjusted for estimated inflation, and are reported as a liability on the Consolidated Statement of Financial Position.

Deferred Revenue

Certain amounts are received pursuant to legislation, regulation or agreement and may only be used in the conduct of certain programs or in the completion of specific work. In addition, certain user charges and fees are collected for which the related services have yet to be performed. These amounts are recognized as revenue in the fiscal year the related expenditures are incurred or services performed.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

Employee Benefits

The contributions to a multi-employer, defined benefit pension plan are expensed when contributions are due.

The costs of termination benefits and compensated absences are recognized when the event that obligates the City occurs; costs include projected future income payments, health care continuation costs and fees paid to independent administrators of these plans, calculated on a present value basis.

The costs of other employee benefits are actuarially determined using the projected benefits method pro-rated on service and management's best estimate of retirement ages of employees, salary escalation, expected health care costs and plan investment performance accrued obligations and related costs of funded benefits are net of plan assets.

Past service costs from plan amendments related to prior period employee services are accounted for in the period of the plan amendment. The effects of a gain or loss from settlements or curtailments are expensed in the period they occur. Net actuarial gains and losses related to employee benefits are amortized over the average remaining service life of the related employee group. Employee future benefit liabilities are discounted using current interest rates on long-term bonds. The costs of workplace safety and insurance obligations are actuarially determined and are expensed.

Government Transfers

Government transfers are recognized in the consolidated financial statements in the period in which events giving rise to the transfer occur, providing the transfers are authorized, any eligibility criteria have been met and reasonable estimates of the amounts can be made.

Reserves and Reserve Funds

Reserves and reserve funds comprise funds set aside for specific purposes by Council and funds which are set aside for specific purposes by legislation, regulation or agreement. For financial reporting purposes, reserve funds set aside by legislation, regulation or agreement are reported as deferred revenue on the Consolidated Statement of Financial Position.

2. Change in Accounting Policy

The City has adopted the new accounting and disclosure requirements for local governments related to liabilities and contingencies as prescribed by PSAB and has applied these requirements on a retroactive basis. As a result, liabilities related to property and liability claims, previously recorded upon payment of a claim, are now reported as liabilities when losses are considered likely and the amounts can be reasonably determined.

The effect of this change has been to increase the 2004 general government expenditures and financing provided by the changes in property and liability claims by \$28,336,000 on the Consolidated Statement of Financial Activities, to increase the 2004 provision for claims included in other liabilities and amounts to be recovered in future years on the Consolidated Statement of Financial Position by \$148,026,000 and to increase the opening 2004 provision for claims and amounts to be recovered in future years by \$119,690,000.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

3. Investments

The cost and market value of the investments reported on the Consolidated Statement of Financial Position as at December 31 are as follows:

| | 2005 | | 2004 | |
|-----------------------------|------------------|----------------------------|------------------|----------------------------|
| | Cost (\$000) | Market Value (\$000) | Cost (\$000) | Market Value (\$000) |
| Federal government bonds | 460,773 | 479,066 | 433,121 | 451,175 |
| Provincial government bonds | 639,072 | 671,033 | 447,872 | 477,448 |
| Municipal government bonds | 403,503 | 430,977 | 391,019 | 419,438 |
| Money market instruments | 434,022 | 434,762 | 654,835 | 657,598 |
| Corporate bonds | 330,588 | 336,137 | 170,527 | 176,840 |
| Other | 322,085 | 323,524 | 275,022 | 270,433 |
| | <u>2,590,043</u> | <u>2,675,499</u> | <u>2,372,396</u> | <u>2,452,932</u> |

The weighted average yield on the cost of the bond investment portfolio during the year was 4.84% (2004 - 5.17%). Maturity dates on investments in the portfolio range from 2006 to 2035. Included in the City's investment portfolio are City of Toronto debentures at coupon rates varying from 4.25% to 8.00% and with a carrying value of \$196,339,000 (2004 - \$156,044,000). Other investments include pooled fixed income and equity funds held by the Toronto Community Housing Corporation ("TCHC") as at December 31, 2005 amounting to \$146,155,000 (2004 - \$137,257,000).

Investments are recorded at the lower of cost or market on a portfolio basis.

4. Note Receivable – Toronto Hydro Corporation

The note receivable from Toronto Hydro Corporation matures on May 6, 2008 and bears interest at a rate of 6.8% per annum (2004 - 6.8%). Subsequent to year end, the maturity date on this note was extended by Council to May 6, 2013. The City has the right to call up to \$330,000,000 of this note during any 12-month period.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

5. Investments in Government Business Enterprises

Government business enterprises consist of Toronto Hydro Corporation, Toronto Parking Authority, TEDCO and Enwave. The City holds an interest of approximately 43% (2004 - 43%) in Enwave and a 100% interest in the other government business enterprises. Details of the continuity of the book value of these investments are as follows:

| | 2005 | 2004 |
|---|------------------|------------------|
| | (\$000) | (\$000) |
| Balance - beginning of year | 1,035,397 | 959,403 |
| Results of operations (Appendix 2) | 102,376 | 112,215 |
| Dividends received (Appendix 2) | (68,000) | (49,200) |
| Elimination of sale of streetlighting | | |
| assets to Toronto Hydro Corporation (Appendix 2) | (60,000) | - |
| Subscription to additional Enwave shares | - | 9,281 |
| | <u>1,009,773</u> | <u>1,031,699</u> |
| Subscription to additional Enwave shares, subsequent to October 31 fiscal year end of Enwave | 2,795 | 3,698 |
| Balance - end of year | <u>1,012,568</u> | <u>1,035,397</u> |

Condensed financial results for each government business enterprise are disclosed in Appendix 2 to these notes to the consolidated financial statements. The results presented in Appendix 2 relate to fiscal years ended December 31 for all government business enterprises except Enwave, whose results are presented based on an October 31 fiscal year end.

The City completed the sale of streetlighting assets to Toronto Hydro Corporation for \$60 million on December 31, 2005. The gain realized by the City on this sale amounted to \$60 million and has been eliminated in these consolidated financial statements. This elimination has reduced the City's share of net equity in Toronto Hydro Corporation as at December 31, 2005 as reflected in the summarized Financial Position in Appendix 2 to these consolidated financial statements and in investments in government business enterprises as reported on the Consolidated Statement of Financial Position.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

Related party transactions between the City and its government business enterprises are as follows:

| | 2005 | 2004 |
|---|---------|---------|
| | (\$000) | (\$000) |
| Received by the City: | | |
| These amounts are included in expenses of the appropriate government business enterprise in the condensed financial results reported in Appendix 2 to these consolidated financial statements | | |
| Interest on note receivable from Toronto Hydro Corporation (Note 4) | 66,656 | 66,656 |
| Share of operating income from Toronto Parking Authority | 30,608 | 36,266 |
| Interest on loans to TEDCO | 9 | 20 |
| Purchased by the City: | | |
| This amount is included in revenues of Toronto Hydro Corporation in the condensed financial results reported in Appendix 2 to these consolidated financial statements. | | |
| Streetlighting electricity and maintenance services from Toronto Hydro Corporation | 14,452 | 14,332 |

6. Deferred Revenue

Revenues received that have been set aside for specific purposes by legislation, regulation or agreement are included in deferred revenue and reported on the Consolidated Statement of Financial Position. Details of these revenues are as follows:

| | 2005 | 2004 |
|------------------------|----------------|----------------|
| | (\$000) | (\$000) |
| Development Charges | 190,313 | 149,179 |
| Water / Wastewater | 155,818 | 99,612 |
| Community Services | 105,260 | 115,546 |
| Third Party Agreements | 83,644 | 61,125 |
| Parkland Acquisition | 72,858 | 53,803 |
| State of Good Repair | 22,830 | 24,705 |
| Planning Act | 7,025 | 5,946 |
| Parking Authority | 6,358 | 6,794 |
| Donations | 2,537 | 2,431 |
| Total | 646,643 | 519,141 |

7. Landfill Closure and Post-Closure Liabilities

The Ontario Environmental Protection Act sets out the regulatory requirements for the closure and maintenance of landfill sites. Under this Act, the City is required to provide for closure and post-closure care of solid waste landfill sites. The costs related to these obligations are provided for over the estimated remaining life of active landfill sites based on usage.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

The City has approximately 161 (2004-149) inactive landfill sites and retains responsibility for all costs relating to closure and post-closure care. The City closed its last remaining active landfill site, Keele Valley, on December 31, 2002, and completed its closure activities on this site during 2005.

Post-closure care activities for landfill sites are expected to occur for a minimum of 40 years and will involve surface and ground water monitoring, maintenance of drainage structures, monitoring leachate and landfill gas, and maintenance of the landfill cover.

The estimated liability for the care of landfill sites is the present value of future cash flows associated with closure and post-closure costs discounted using the City's average long-term borrowing rate of 5% (2004 - 5.5%). The estimated present value of future expenditures for closure and post-closure care as at December 31, 2005 is \$125,025,000 (2004 - \$114,591,000).

In order to help reduce the future impact of these obligations, the City has established a reserve fund for the care of these sites and maintains a trust fund in satisfaction of requirements of the Ministry of the Environment. The balance in the solid waste management perpetual care reserve fund as at December 31, 2005 was \$33,998,000 (2004 - \$31,938,000) and is included as part of State of Good Repair reserve fund in Appendix 1, and the balance in the Keele Valley Site Post-Closure Trust Fund as at December 31, 2005 was \$6,885,000 (2004 - \$6,744,000) (Note 14).

8. Mortgages Payable

The mortgages payable are obligations of TCHC which has provided a security interest in the housing properties owned by TCHC. These properties have a net book value of \$1,362,475,000 (2004 - \$1,382,537,000) and have not been reflected in the Consolidated Statement of Financial Position.

Interest rates of the mortgages range from 4.4% to 13.3%. Principal repayments relating to the mortgages outstanding as at December 31, 2005 are due as follows:

| | \$000 |
|------------|----------------|
| 2006 | 28,544 |
| 2007 | 30,197 |
| 2008 | 31,930 |
| 2009 | 33,653 |
| 2010 | 35,715 |
| Thereafter | 805,357 |
| | <u>965,396</u> |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

9. Net Long-Term Debt

Provincial legislation restricts the use of long-term debt to finance only capital expenditures. Provincial legislation allows the City to issue debt on behalf of the Toronto School Boards at the request of these boards. The responsibility of raising the amounts to service these liabilities lies with the respective school board. The debt is a direct, joint and several obligation of the City and the school boards.

Net long-term debt reported on the Consolidated Statement of Financial Position comprises the following:

| | 2005 (\$000) | 2004 (\$000) |
|--|------------------|------------------|
| Long-term debt issued by the City at various rates of interest ranging from 3.65% to 8.65% | 2,443,505 | 2,110,465 |
| Loans payable to the Province of Ontario at 2.76% | 170,171 | 175,331 |
| Loan payable bearing interest at 8.05% | 1,652 | 1,718 |
| Sinking fund deposits | (650,207) | (606,822) |
| | <u>1,965,121</u> | <u>1,680,692</u> |

Principal repayments relating to net long-term debt of \$1,965,121 outstanding as at December 31, 2005 are due as follows:

| | \$000 |
|------------|------------------|
| 2006 | 274,329 |
| 2007 | 250,831 |
| 2008 | 239,030 |
| 2009 | 231,183 |
| 2010 | 207,771 |
| Thereafter | 761,977 |
| | <u>1,965,121</u> |

Included in net long-term debt are outstanding debentures of \$1,888,000,000 (2004 - \$1,678,000,000) for which there are sinking fund assets with a carrying value of \$666,371,000 (market value - \$720,965,000 (2004 - \$627,680,000 (market value - \$668,187,000))). Sinking fund assets are comprised of short-term notes and deposits, government and government-guaranteed bonds and debentures and corporate bonds. Government and government-guaranteed bonds and debentures include City of Toronto debentures with a carrying value of \$146,357,000 (market value - \$154,106,000) (2004-\$163,087,000 (market value - \$171,190,000)).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

The City's long-term liabilities at the end of the year are to be recovered from the following sources:

| | 2005 | 2004 |
|-------------------------------|------------------|------------------|
| | (\$000) | (\$000) |
| Property taxes | 1,904,772 | 1,603,207 |
| Water billings | 2,328 | 4,782 |
| Toronto District School Board | 58,021 | 72,703 |
| | <u>1,965,121</u> | <u>1,680,692</u> |

10. Employee Benefit Liabilities

The City provides certain benefits, including retirement and other post-employment benefits, to most of its employees. Employee benefit liabilities as at December 31 are as follows:

| | 2005 | 2004 |
|--|------------------|------------------|
| | (\$000) | (\$000) |
| Future payments required for: | | |
| Pension liabilities, other than OMERS | 95,442 | 103,763 |
| Sick leave benefits | 308,308 | 298,884 |
| Workplace Safety and Insurance Board obligations | 289,225 | 281,135 |
| Other employment and post-employment benefits | 1,547,001 | 1,434,447 |
| Total employee benefit obligation | <u>2,239,976</u> | <u>2,118,229</u> |
| Less: Unamortized actuarial loss | 127,688 | 140,454 |
| Employee benefit liabilities | <u>2,112,288</u> | <u>1,977,775</u> |

The continuity of the City's employee benefit liabilities, in aggregate, is as follows:

| | 2005 | 2004 |
|--------------------------------|------------------|------------------|
| | (\$000) | (\$000) |
| Balance – beginning of year | 1,977,775 | 1,791,750 |
| Current service cost | 132,502 | 144,906 |
| Interest cost | 117,572 | 112,198 |
| Cost of plan amendments | - | 29,144 |
| Amortization of actuarial loss | 21,410 | 20,990 |
| Expected benefits paid | (136,971) | (121,213) |
| Balance – end of year | <u>2,112,288</u> | <u>1,977,775</u> |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

The total expenditures related to these employee benefits include the following components:

| | 2005 | 2004 |
|--------------------------------|-----------------------|-----------------------|
| | (\$000) | (\$000) |
| Current period benefit cost | 132,502 | 144,906 |
| Amortization of actuarial loss | 21,410 | 20,990 |
| Interest cost | 117,572 | 112,198 |
| Total expenditures | <u>271,484</u> | <u>278,094</u> |

Pension Plans

The City makes contributions to the Ontario Municipal Employees' Retirement System ("OMERS") plan, a multi-employer pension plan, on behalf of most of its employees. The plan is a defined benefit plan that specifies the amount of the retirement benefit to be received by the employees based on length of service and rates of pay. Employees and employers contribute jointly to the plan.

Because OMERS is a multi-employer pension plan, any pension plan surpluses or deficits are a joint responsibility of all Ontario municipalities and their employees. As a result, the City does not recognize any share of the OMERS pension surplus or deficit. Employer contributions for current service amounted to \$101,484,000 (2004 - \$87,941,000) and are matched by employee contributions in a similar amount.

The amount contributed for past service to OMERS for the year ended December 31, 2005 was \$405,000 (2004 - \$161,000). Employer's contributions for current and past service are included as an expenditure on the Consolidated Statement of Financial Activities.

The Toronto Transit Commission also participates in a multi-employer pension plan, on behalf of most of its employees. The plan is a defined benefit/defined contribution hybrid pension plan that provides pensions to members based on the length of service and average base year (pensionable) earnings. Employer contributions to this plan during 2005 amounted to \$45,033,000 (2004 - \$42,900,000).

The City also sponsors five defined benefit pension plans that provide benefits to employees who were employed prior to the establishment of the OMERS pension plan. The plans cover closed groups of employees hired prior to July 1, 1968 and provide for pensions based on length of service and final average earnings.

The plans provide increases in pensions to retirees and their spouses to the extent that an actuarial surplus is available. As at December 31, 2005, there were 36 (2004 - 60) active members with an average age of 60. There were also 5,996 (2004 - 6,319) pensioners and 2,884 (2004 - 2,889) spousal beneficiaries in receipt of a pension, with an average age of 74. Pension payments and refunds during the year were approximately \$200,827,000 (2004 - \$205,355,000).

Employees contribute a portion (varying amounts ranging from 5% to 9.8%) of their salary to the pension plans for current service and the City contributes an equal amount. Member contributions cease upon completion of 35 years of service.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

While the City and employees are required to contribute equal amounts into the pension plans, the City retains the risk of the accrued benefit obligation. The pension plan assets are invested in Canadian and foreign equities, bonds and debentures and other short-term investments.

One of the plans, the Toronto Civic Employees Pension Plan, is in a surplus position. The accrued benefit asset of this plan as at December 31 includes the following components:

| | 2005 (\$000) | 2004 (\$000) |
|--|-----------------------|-----------------------|
| Accrued benefit obligation – end of year | 397,899 | 412,829 |
| Pension plan assets – end of year | <u>475,306</u> | <u>461,714</u> |
| Net pension assets | 77,407 | 48,885 |
| Unamortized actuarial losses | <u>52,954</u> | <u>81,055</u> |
| Accrued benefit asset | <u>130,361</u> | <u>129,940</u> |

Since there is uncertainty about the City's right to this accrued benefit asset, this amount has not been reflected on the Consolidated Statement of Financial Position.

The remaining four plans are in a deficit position. The accrued benefit asset of two of these plans, the Metro Toronto Employees Pension Plan and the Toronto Firefighters Pension Plan, includes the following components as at December 31:

| | 2005 (\$000) | 2004 (\$000) |
|--|-----------------------|-----------------------|
| Accrued benefit obligation – end of year | 1,146,423 | 1,173,879 |
| Pension plan assets – end of year | <u>1,087,376</u> | <u>1,081,147</u> |
| Net pension liability | (59,047) | (92,732) |
| Unamortized actuarial losses | <u>214,229</u> | <u>269,631</u> |
| Accrued benefit asset | <u>155,182</u> | <u>176,899</u> |

The accrued benefit asset of the above two plans has not been reflected on the Consolidated Statement of Financial Position as the City will not realize any future benefit from this asset.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

The accrued pension liability of the two remaining pension plans, the York Civic Employees Pension Plan and the Toronto Police Pension Plan, is included in employee benefit liabilities on the Consolidated Statement of Financial Position as at December 31 and includes the following components:

| | 2005 (\$000) | 2004 (\$000) |
|---|------------------|------------------|
| Accrued benefit obligation – end of year | 886,580 | 903,909 |
| Pension plan assets – end of year | 754,620 | 728,279 |
| Net pension liability | (131,960) | (175,630) |
| Unamortized actuarial losses | 36,518 | 71,867 |
| Accrued pension liability | (95,442) | (103,763) |

Actuarial valuations for funding purposes for each of the five plans are carried out annually using the projected benefit method pro-rated on service. The most recent actuarial funding reports were prepared as at December 31, 2004, with the results extrapolated to December 31, 2005. The accrued benefit obligation as at December 31, 2005 is based on actuarial valuations for accounting purposes as at December 31, 2005. The unamortized actuarial losses in the five plans are being amortized on a straight-line basis. As most of the members are no longer active, the actuarial losses are being amortized over a 10 to 13 year period, being the expected average remaining life expectancy of the inactive members.

The actuarial valuations were based on a number of assumptions about future events, such as inflation rates, interest rates, wage and salary increases and employee turnover and mortality. The assumptions used reflect the City's best estimates. The inflation rate is estimated at 3% per annum (2004 – 3%) and the rate of compensation increase is estimated at 4% per annum (2004 – 3.5%) for determining the accrued benefit obligation and benefit cost. The discount rate used to determine the accrued benefit obligation is 5% (2004 – 5.6%) and benefit cost is 5.6% (2004 – 6%) per annum.

Pension plan assets are valued at market values. The expected rate of return on plan assets is 6.75% (2004 – 7%) per annum net of all administrative expenses. The return on the market value of plan assets during the year was 11.2% (2004 – 9.9%).

Total expenditures (recoveries) related to the two pensions in an accrued pension liability position include the following components:

| | 2005 (\$000) | 2004 (\$000) |
|---|-----------------|-----------------|
| Current period benefit cost | - | 15 |
| Amortization of actuarial losses | 7,691 | 13,267 |
| Interest cost on the average accrued benefit obligation | 48,590 | 57,342 |
| Expected return on average pension plan assets | (47,298) | (49,227) |
| Net expenditures related to pension plans | 8,983 | 21,397 |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

The net expenditures related to the pension plans in an accrued liability position are included in the Consolidated Statement of Financial Activities as a component of expenditures.

Vested Sick Leave Benefit Liability

Under the sick leave benefit plan, employees are credited with a maximum of 18 days sick time per annum. Unused sick leave can accumulate and employees may become entitled to a cash payment, capped at one half of unused sick time to a maximum of 130 days when they leave the City's employment. The liability for the accumulated sick leave represents the extent to which sick leave benefits have vested and could be taken in cash by employees on termination. A sick leave reserve fund is established to help reduce the future impact of these obligations. As at December 31, 2005 the balance in the sick leave reserve fund is \$77,699,000 (2004 - \$83,018,000) and is included as part of Employee Benefits reserve fund in Appendix 1. Payments during the year amounted to \$19,556,000 (2004 - \$18,963,000).

Workplace Safety and Insurance Board Obligations

The City is a Schedule 2 employer under the Workplace Safety and Insurance Act and, as such, assumes responsibility for financing its workplace safety insurance costs. The accrued obligation represents the actuarial valuation of claims to be insured based on the history of claims with City employees. A Workers' Compensation reserve fund is established to help reduce the future impact of these obligations. As at December 31, 2005 the balance in the Workers' Compensation reserve fund is \$9,919,000 (2004 - \$10,780,000) and is included as part of Employee Benefits reserve fund in Appendix 1. Payments during the year by the City to the Workplace Safety and Insurance Board amounted to \$26,505,000 (2004 - \$25,443,000).

Other Employment and Post-Employment Benefits

The City provides health, dental, life insurance and long-term disability benefits to certain employees. The accrued liability represents the actuarial valuation of benefits to be paid based on the history of claims with City employees. An employee benefits reserve fund is established to help reduce the future impact of these obligations. As at December 31, 2005 the balance in the employee benefits reserve fund is \$139,370,000 (2004 - \$144,431,000) and is included as part of Employee Benefits reserve fund in Appendix 1. Payments during the year amounted to \$17,229,000 (2004 - \$20,642,000).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

Due to the complexities in valuing the plans, actuarial valuations are conducted on a periodic basis. The liabilities reported in these consolidated financial statements are based on the most recent actuarial valuations as at December 31, 2002, with the results extrapolated to December 31, 2005. Many of the estimates and assumptions used may change significantly with the next detailed valuation. The significant actuarial assumptions adopted in measuring the City's accrued benefit obligations and benefit costs for other retirement and post-employment benefits are as follows:

| | 2005 | 2004 |
|---|-------|-------|
| Discount rate for accrued benefit obligation and benefit costs: | | |
| Post employment | 5.5% | 5.5% |
| Post retirement, sick leave and WSIB | 6.0% | 6.0% |
| Rate of compensation increase | 3% | 3% |
| Health care inflation – Hospital, dental care and other medical | 4.5% | 4.5% |
| Health care inflation – Drugs | 11.3% | 12.0% |

The health care inflation rate for drugs is assumed to reduce to 5.5% over 10 years.

11. Amounts to be Recovered in Future Years

Amounts to be recovered in future years comprise the gross amounts of the following liabilities as at December 31, some of which have been partially funded through reserve funds:

| | 2005 (\$000) | 2004 (\$000) |
|--|------------------|------------------|
| TCHC mortgages (Note 8) | 965,396 | 992,571 |
| Net long-term debt (Note 9) | 1,965,121 | 1,680,692 |
| Employee benefit liabilities (Note 10) | 2,112,288 | 1,977,775 |
| Property and liability claims provisions (Note 16) | 160,068 | 148,026 |
| Landfill closure and post-closure liabilities (Note 7) | 125,025 | 114,591 |
| | <u>5,327,898</u> | <u>4,913,655</u> |
| Less amounts recoverable from Toronto District School Board (Note 9) | 58,021 | 72,703 |
| | <u>5,269,877</u> | <u>4,840,952</u> |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

12. Capital Fund

The balance of the Capital Fund, reported on the Consolidated Statement of Financial Position, represents the net financial position of all uncompleted capital projects as at December 31 and is analyzed as follows:

| | 2005 (\$000) | 2004 (\$000) |
|--|-------------------------|-------------------------|
| Capital financing received in advance of expenditures | 132,793 | 214,803 |
| Capital expenditures yet to be financed | <u>(377,952)</u> | <u>(579,623)</u> |
| Capital Fund Balance (Schedule 2) | <u>(245,159)</u> | <u>(364,820)</u> |
| Capital expenditures yet to be financed are to be funded in future years as follows: | | |
| Long-term liabilities | 343,886 | 530,294 |
| Developer recoveries and reserves | 28,346 | 30,964 |
| Other | 5,720 | 18,365 |
| | <u>377,952</u> | <u>579,623</u> |

Approval has been received for future issuance of \$416,237,000 in long-term liabilities, which includes the \$343,886,000 noted above. The remaining \$72,351,000 in approved long-term debt is for capital expenditures yet to be incurred.

13. Expenditures by Object

Expenditures by object comprise the following:

| | 2005 (\$000) | 2004 (\$000) |
|------------------------------|-------------------------|-------------------------|
| Salaries, wages and benefits | 3,671,156 | 3,542,407 |
| Materials | 1,944,301 | 2,045,172 |
| Contracted services | 1,042,994 | 842,376 |
| Interest on long-term debt | 130,098 | 111,873 |
| Transfer payments | 429,032 | 330,729 |
| Other | 893,524 | 906,088 |
| | <u>8,111,105</u> | <u>7,778,645</u> |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

14. Trust Funds

Trust funds administered by the City amounting to \$48,704,000 (2004 - \$47,965,000) have not been included on the Consolidated Statement of Financial Position nor have their operations been included on the Consolidated Statement of Financial Activities. Trust fund balances as at December 31 are as follows:

| | 2005 | 2004 |
|---|---------------|---------------|
| | (\$000) | (\$000) |
| Toronto Atmospheric Trust Fund | 26,425 | 24,444 |
| Keele Valley Site Post-Closure (Note 7) | 6,885 | 6,744 |
| Homes for the Aged – Residents | 6,323 | 6,404 |
| Development Charges Trust – Railway Lands | 3,094 | 2,479 |
| Community Services Levies | 1,025 | 998 |
| Police Trust Funds | 994 | 1,001 |
| Contract Aftercare | 965 | 948 |
| Waterpark Place | 915 | 891 |
| Candidates' Municipal Election Surpluses | 693 | 654 |
| Development Charges Trust – Queen's Quay | 459 | 446 |
| Heritage and Culture Trusts | 357 | 348 |
| Lakeshore Pedestrian Bridge | 210 | 204 |
| Children's Greenhouse – Allan Gardens | 103 | 100 |
| Ontario Home Renewal Program | 46 | 397 |
| Other trust funds | 210 | 185 |
| Library Trusts | - | 1,722 |
| | <u>48,704</u> | <u>47,965</u> |

15. Budget Data

Budget data for 2005 included in these consolidated financial statements represents budgets approved by Council except for reserves and reserve funds, which have been modified to reflect funding contributions contained in approved operating and capital budgets.

16. Contingencies and Commitments

The City is subject to various litigations and claims arising in the normal course of its operations. The final outcome of the outstanding claims cannot be determined at this time. However, management believes that the ultimate disposition of these matters will not materially exceed the amounts recorded in the accounts.

Exposures on property and liability claims are covered by a combination of self-insurance and coverage with insurance carriers. Provisions for property and liability claims are recorded in other liabilities on the Consolidated Statement of Financial position in the amount of \$160,068,000 (2004-\$148,026,000).

A class action was commenced against the former Toronto Hydro-Electric Commission and other Ontario municipal electric utilities under the Class Proceedings Act, 1992 seeking \$500,000,000 in restitution for late payment charges collected by them from their customers that were in excess of the interest limit stipulated in section 347 of the Criminal Code. This action is at a preliminary stage. Pleadings have closed but examinations for discovery have not been conducted and the classes have not been certified.

A similar class action was commenced against the Toronto Hydro-Electric Commission under the Class Proceedings Act, 1992 seeking \$64,000,000 in restitution for late payment charges collected by it from its customers that were in excess of the interest limit stipulated in section 347 of the Criminal Code. This action

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

is also at the preliminary stage. Pleadings have closed and examinations for discovery have been conducted but, as in the first action, the classes have not been certified.

Given the preliminary status of these actions, it is not possible at this time to quantify the effect, if any, of these actions on these consolidated financial statements.

A class action in the amount of \$11,000,000 in general and special damages was commenced against the City following an outbreak of Legionnaire's Disease in 2005 at Seven Oaks, one of the City's Homes for the Aged. The action alleges improper maintenance of the facility's air conditioning/cooling tower but has not proceeded to the stage involving the motion of certification. At this preliminary stage, it is not possible to quantify the effect, if any, of this action on these consolidated financial statements.

A class action claiming \$500,000,000 in damages, plus interest and costs, was served on the Toronto Transit Commission on November 30, 2001. The claim is based on alleged exposure by workers to asbestos during construction work at the Sheppard Subway Station. The claim also names the Ministry of Labour and an environmental consultant company as defendants and alleges various violations of the Occupational Health and Safety Act and its regulations. The action has not proceeded to the stage involving the motion of certification. Management believes that the ultimate disposition of the matter will not materially exceed amounts recorded in the accounts.

In February 2005 a contract was awarded amounting to \$209,600,000 for the purchase of an additional 330 buses with delivery in 2006 and 2007. At December 31, 2005 the Toronto Transit Commission has various capital project contractual commitments of \$63,600,000 (2004 - \$50,100,000).

The Ministry of the Environment has issued Certificates of Approval for 14 (2004 - 11) of the estimated 161 (2004 - 149) inactive landfill sites. Applications for Certificates of Approval at other inactive sites may be required prior to the commencement of any remediation work. It is not possible to quantify the effect, if any, of this request on these consolidated financial statements beyond those amounts recorded as landfill closure and post-closure liabilities (Note 7).

The City has provided unconditional loan guarantees to certain third parties amounting to \$30,885,000 (2004 - \$40,190,000), primarily related to possible defaults in financial agreements for certain construction projects and for several cultural non-profit organizations.

As at December 31, 2005, the City is committed to future minimum annual operating lease payments for premises and equipment as follows:

| | \$000 |
|------------|----------------|
| 2006 | 26,661 |
| 2007 | 22,286 |
| 2008 | 17,404 |
| 2009 | 11,779 |
| 2010 | 9,156 |
| Thereafter | 46,621 |
| | <u>133,907</u> |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2005

17. Public Sector Salary Disclosure Act 1996

The Public Sector Salary Disclosure Act, 1996 (the "Act") requires the disclosure of the salaries and benefits of employees in the public sector who are paid a salary of \$100,000 or more in a year. The City complies with the Act by providing the information to the Ontario Ministry of Municipal Affairs and Housing for disclosure on the public website at www.fin.gov.on.ca.

18. Comparative Consolidated Financial Statements

These consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the 2005 consolidated financial statements. Included in the comparative amounts presented in these consolidated financial statements are restatements for errors in the estimate of solid waste landfill obligations and in the conversion of accounts of a consolidated entity from the commercial to the municipal basis of accounting.

Estimates of solid waste landfill estimates were understated in prior years due to a calculation error. The effect of a restatement for this error has been to increase landfill closure and post-closure liabilities by \$16,358,000 as at December 31, 2004 (2003 - \$17,585,000), to increase amounts to be recovered in future years by \$16,358,000 as at December 31, 2004 (2003 - \$17,585,000), to decrease 2004 environmental services expenditures by \$1,227,000 and to decrease 2004 financing provided by changes in solid waste landfill obligations by \$1,227,000.

In addition, errors in the conversion of the accounts of Toronto Community Housing Corporation, a consolidated entity, have resulted in the overstatement of revenues and accounts receivable in the consolidated financial statements for 2002, 2003 and 2004. The effect of a restatement for these errors in these consolidated financial statements has been to reduce accounts receivable as at December 31, 2004 by \$23,693,000, to increase the opening 2004 operating fund balance by \$814,000 and to reduce other revenues by \$24,507,000.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - APPENDIX 1

December 31, 2005

Details of reserves and reserve funds

| | 2005 | 2004 |
|-----------------------|----------------|----------------|
| | (\$000) | (\$000) |
| RESERVES | | |
| Vehicle and Equipment | 101,274 | 79,423 |
| Working Capital | 79,395 | 79,395 |
| Water and Wastewater | 14,755 | 17,999 |
| Other reserves | 1,061 | 1,984 |
| | <u>196,485</u> | <u>178,801</u> |
| RESERVE FUNDS | | |
| Employee Benefits | 227,025 | 238,264 |
| Stabilization | 122,990 | 162,591 |
| Corporate | 216,150 | 183,626 |
| Community Initiatives | 54,646 | 48,248 |
| State of Good Repair | 73,601 | 67,399 |
| | <u>694,412</u> | <u>700,128</u> |
| | <u>890,897</u> | <u>878,929</u> |

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - APPENDIX 2
December 31, 2005

Government Business Enterprises
Condensed Financial Results (\$'000)

| Fiscal Year Ended | Toronto Hydro Corporation December 31 | | Toronto Parking Authority December 31 | | TEDCO December 31 | | Enwave October 31 | | Total | |
|---|---|-----------|---|---------|----------------------|--------|----------------------|---------|-----------|-----------|
| | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 |
| Financial Position | | | | | | | | | | |
| Assets | | | | | | | | | | |
| Current | 1,061,085 | 871,944 | 20,273 | 16,032 | 10,582 | 9,461 | 7,347 | 7,256 | 1,099,287 | 904,693 |
| Capital | 1,624,741 | 1,547,557 | 116,343 | 107,722 | 30,859 | 31,496 | 232,069 | 220,244 | 2,004,012 | 1,907,019 |
| Other | 133,432 | 172,233 | 21,975 | 27,952 | 35,421 | 32,770 | 12,319 | 8,826 | 203,147 | 241,781 |
| | 2,819,258 | 2,591,734 | 158,591 | 151,706 | 76,862 | 73,727 | 251,735 | 236,326 | 3,306,446 | 3,053,493 |
| Liabilities | | | | | | | | | | |
| Current | 941,211 | 701,636 | 19,985 | 23,352 | 7,319 | 5,573 | 19,800 | 23,354 | 988,315 | 753,915 |
| Long-term | 1,032,180 | 1,068,676 | - | - | 58,781 | 55,845 | 58,670 | 51,157 | 1,149,631 | 1,175,678 |
| | 1,973,391 | 1,770,312 | 19,985 | 23,352 | 66,100 | 61,418 | 78,470 | 74,511 | 2,137,946 | 1,929,593 |
| Net equity | 845,867 | 821,422 | 138,606 | 128,354 | 10,762 | 12,309 | 173,265 | 161,815 | 1,168,500 | 1,123,900 |
| City's share (Note 5) | *785,867 | 821,422 | 138,606 | 128,354 | 10,762 | 12,309 | 74,538 | 69,614 | 1,009,773 | 1,031,699 |
| Results of Operations | | | | | | | | | | |
| Revenues | 2,626,671 | 2,241,799 | 94,376 | 97,856 | 9,198 | 8,678 | 59,070 | 51,820 | 2,789,315 | 2,400,153 |
| Expenses | 2,534,226 | 2,140,911 | 84,124 | 88,384 | 10,745 | 7,997 | 56,220 | 49,090 | 2,685,315 | 2,286,382 |
| Net income (loss) | 92,445 | 100,888 | 10,252 | 9,472 | (1,547) | 681 | 2,850 | 2,730 | 104,000 | 113,771 |
| City's share (Note 5) | 92,445 | 100,888 | 10,252 | 9,472 | (1,547) | 681 | 1,226 | 1,174 | 102,376 | 112,215 |
| Dividends paid (Note 5) | 68,000 | 49,200 | - | - | - | - | - | - | 68,000 | 49,200 |
| Net Book Value Of Assets Sold From The City To Hydro (Note 5) | *60,000 | - | - | - | - | - | - | - | 60,000 | - |

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