



STAFF REPORT ACTION REQUIRED

2008 Audited Consolidated Financial Statements

Date:	September 2, 2009
To:	Audit Committee
From:	Deputy City Manager and Chief Financial Officer Acting Treasurer
Wards:	All
Reference Number:	P:\2009\Internal Services\acc\ac09011acc (AFS# 8703)

SUMMARY

The purpose of this report is to present the City of Toronto's Consolidated Financial Statements for the year ended December 31, 2008 to Council for approval and provide highlights of the City's 2008 financial performance and financial condition as of December 31, 2008.

RECOMMENDATIONS

The Deputy City Manager and Chief Financial Officer and Acting Treasurer recommend that:

1. The 2008 Consolidated Financial Statements as attached in Appendix A be approved.

Financial Impact

There are no financial implications as a result of this report.

DECISION HISTORY

Annually, as required by the Sections 231 and 232 of the *City of Toronto Act*, the City prepares and publishes an annual financial statement that consolidates the financial results of all City divisions and the agencies, boards, commissions and government business enterprises that the City controls.

ISSUE BACKGROUND

The Consolidated Financial Statements are intended to provide Council, the public, the City's debenture holders, and other stakeholders, an overview of the state of the City's

finances at the end of the fiscal year and indicate revenues, expenses and funding for the year.

The preparation, content and accuracy of the Consolidated Financial Statements and all other information included in the financial report are the responsibility of management. As required under Section 231 of the *City of Toronto Act*, the financial statements are prepared in accordance with generally accepted accounting principles as set by the Canadian Institute of Chartered Accountant's (CICA) Public Sector Accounting Board (PSAB).

These Consolidated Financial Statements have been audited by Ernst & Young LLP whose role is to express an independent opinion on the fair presentation of the City's financial position and operating results and to confirm that the statements are free from material misstatement. The external auditor's opinion is to provide comfort to third parties that the financial statements can be relied upon.

The Consolidated Financial Statements include the following individual statements:

<u>Name</u>	<u>Purpose</u>
Consolidated Statement of Financial Position	Provides a summary of the City's financial assets and liabilities (the financial resources the City has available for future services and the future revenues required to pay for past transactions).
Consolidated Statement of Financial Activities	Outlines revenues, expenditures and financing in the year, as well as fund balances at year end. 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 revenues, expenditures and financing for current operations in the year with comparisons to budget, as well as fund balances at year end.
Analysis of Capital Operations	Outlines revenues, expenditures and financing for capital operations in the year with comparisons to budget, as well as fund balances at year end.
Analysis of Reserves and Reserve Funds	Summarizes funds raised by the City in the year for reserve and reserve funds, what those funds were used for and how they compared to the budget.

The Consolidated Financial Statements combine the financial results of the City's divisions with the financial results of the agencies, boards, commissions and government business enterprises that the City effectively controls. There are 108 entities that are included in the financial statements and these are listed in Note 1 to the Consolidated Financial Statements. The remaining notes to the 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 readers in understanding the financial statements, schedules have been prepared for current operations, capital operations, and reserves and reserve funds.

At its meeting held on July 10, 2008 the Audit Committee, in its consideration of the City's 2007 Consolidated Financial Statements, requested staff to move towards a plain language approach when submitting future Financial Statements. Various sections of this report and the notes to this year's Consolidated Financial Statements have been written to incorporate plainer language. As generally accepted accounting principles require specific disclosures, and as certain items are complex, on occasion this limits management's ability to simplify the language. However, as additional statements are prepared and feedback is received, it is expected that the readability of these statements will continue to improve.

Consolidated Statement of Financial Position

The Consolidated Statement of Financial Position is the municipal equivalent of the private sector's balance sheet with the exception that tangible capital (physical) or "fixed" assets are not recorded. As indicated in Note 20 to the Consolidated Financial Statements, beginning in 2009, Tangible Capital Assets will be reported on this statement. This statement focuses on the City's assets and liabilities. The difference between the two is the City's net liability position and represents the net amount that must be financed from future budgets. The City's net liabilities are broken down in the "Municipal Position" portion of the statement and are divided between the funds (assets) 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:

- (a) The *Operating Fund* is primarily made up of the City's financial interest in its government business enterprises, which consist of Toronto Hydro Corporation, Toronto Parking Authority, TEDCO (prior to November 14, 2008) 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 (TAF) are the most prominent. The Operating Fund also contains the 2008 surplus which will be distributed in 2009 in accordance with the 2009 Budget.

- (b) The *Capital Fund* represents the net position of the City's capital projects. The capital fund is in a deficit position, which indicates that financing (such as a debt issuance) for certain projects has yet to occur.
- (c) 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 expenditure and revenue levels from year to year. A breakdown of the City's reserves and reserve funds can be found in Note 15 to the Consolidated Financial Statements.

In addition to the reserves and reserve funds, the City also has received funds for specific purposes under legislation, regulation or agreements. The recognition of these funds as revenues has been deferred until related expenditures occur in the future. For example, development charges, parkland dedication fees and Federal and Provincial Government transfers received (such as public transit funding), are not recognized as revenues until such time as the projects are constructed. These restricted funds are included in Financial Liabilities and not in the Municipal Position. A breakdown of the City's deferred revenue obligatory reserve funds can be found in Note 6(a) to the Consolidated Financial Statements.

Consolidated Statement of Financial Activities

The Consolidated Statement of Financial Activities is considered to be the municipal equivalent to the private sector's income statement. However, like the Consolidated Statement of Financial Position, there is an important distinction. Although the statements are on an accrual basis of accounting for most revenues and expenses, this is not a "full accrual" model as the costs of the City's physical assets are expensed in the year they are purchased or constructed. As indicated in Note 20 to the Consolidated Financial Statements, this will change for the 2009 reporting period when capital assets will be amortized over the expected useful lives of the assets and amortization expense will be recorded in the statement.

The Consolidated Statement of Financial Activities provides a summary of the revenues, expenditures and financing activities throughout the reporting period and reflects the combined operations of the operating, capital, reserve and reserve funds for the City and its consolidated entities.

The focus of the Consolidated Statement of Financial Activities is the net expenditure/revenue figure found in the middle of the statement. A net expenditure (referred to in the statement as an "Excess of Expenditures over Revenues") 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, solid waste obligation) in the year and the debt retired in the year.

Restatement of Prior Period (2007) Consolidated Financial Statements

Prior to preparation of the 2008 consolidated financial statements, management reviewed the following two items and jointly with Ernst & Young determined that restatement of the 2007 comparative figures is appropriate.

Actuarial valuation of sick leave liability

Actuarial valuations of all employee benefit liabilities are conducted on a periodic basis by an actuary engaged by the City. The last actuarial review was completed in 2007 for year end 2006, and extrapolated to December 31, 2007 and 2008. During 2009, the City identified an error in the actuarial valuation of sick leave liabilities. As a result, the actuary prepared a revised valuation and the employee benefit liabilities were restated for 2007 resulting in:

- an increase in the employee benefit obligation of \$200.8 million;
- an increase in the unamortized actuarial loss of \$132.0 million; and
- a net increase in the accrued benefit liabilities of \$68.8 million.

This error was discovered in advance of labour negotiations and staff were using the most current information during bargaining and the reporting of results.

There is no change in the operating fund balance as a result of this restatement given that the increase in operating expenditures is offset by the changes in employee benefit liabilities recognized in financing and transfers.

Proportionate Consolidation of the Toronto Waterfront Revitalization Corporation (TWRC)

During the year management became aware of a change in the organizational structure of TWRC from a provincially controlled entity to a corporation without share capital, with the City, Provincial and Federal governments each contributing one third of the capital required for TWRC priority projects. As a result, the 2007 consolidated financial statements have been restated to proportionately consolidate the City's one-third share of TWRC. This is the same accounting treatment used by the Province. Prior to the restatement, only amounts paid to and received from the TWRC were recorded as expenditures or revenues, on an accrual basis, in the City's consolidated financial statements. This restatement resulted in a decrease in net expenditures of \$6.1 million in 2007.

COMMENTS

The City's 2008 Consolidated Financial Statements presented in Appendix A of this report provide details of the state of the City's finances at the end of the fiscal year, and the revenues and expenses for the year ended December 31, 2008.

2008 Financial Highlights

- The City collected consolidated revenues of \$9.51 billion (2007 - \$8.86 billion) and spent \$9.96 billion (2007 - \$9.47 billion) for a net consolidated expenditure of \$451 million (2007 - \$606 million).
- The City's net liabilities increased by \$444 million to \$3.33 billion (2007 - \$2.89 billion).
- Capital spending for the year was \$1.96 billion (2007 - \$1.86 billion).
- The level of unfinanced capital expenditure increased by \$431 million to \$589 million (2007 - \$158 million).
- Cash and investments increased \$337 million to \$4.05 billion (2007 - \$3.71 billion).
- The City's investment in its government business enterprises increased by \$51 million to \$1.19 billion (2007 - \$1.14 billion).
- Deferred Revenue increased by \$684 million to \$1.92 billion (2007 - \$1.24 billion)
- Net long-term debt to third parties decreased by \$17 million to \$2.74 billion (2007 - \$2.76 billion).
- Mortgage debt obligations of Toronto Community Housing Corporation declined by \$30 million to \$869 million (2007 - \$899 million).
- The employee benefits liability increased by \$188 million to \$2.59 billion (2007 - \$2.40 billion).

Reconciliation to the Operating Budget Surplus

The following schedule reconciles the “accounting surplus (deficit)” reported in the Consolidated Financial Statements to the cash based “operating budget surplus (deficit)” reported in the budget variance reports to the Budget Committee for budgeting and rate setting purposes.

The “accounting surplus (deficit)” is represented by the increase (decrease) in the Operating Fund as shown in Schedule 1 of the financial statements and reconciles to the surplus reported for budget purposes as follows:

	<i>(in thousands of dollars)</i>	
	2008	2007
Surplus as reported in 2008 Final Year-end Operating Variance Report	79,526	95,137
Additional Year End Adjustments / Accruals (based on actuals vs. estimates) (see Note 1 below)	29,875	(11,696)
Final 2008 Operating Budget Surplus (City ONLY)	109,401	83,441
Accounting Adjustments for Financial Statement Presentation Purposes		
Transfer to reserve fund – principal repayment of Note Receivable –Toronto Hydro Corporation	-	(245,000)
Non cash adjustments to the ABC surpluses reported in the Consolidated Statement of Financial Activities	70,713	93,857
Net increase in City's equity in Government Business Enterprises (GBE's) (Toronto Hydro, TEDCO, Enwave, Toronto Parking Authority)	51,285	61,709
Prior Year Surplus carried forward and distributed in the Current Year Budget	(95,137)	(142,577)
PSAB Adjustments including adjustment for TCHC debt expense and employee benefits for future years (See Note 2 below)	(116,486)	10,426
(Decrease)/ Increase in Operating Fund Balance for the year as reported on the Analysis of Consolidated Current Operations - Schedule 1	19,776	(138,144)

Note 1: Increase in "Additional Year End Adjustments / Accruals" is mainly due to:

- accrual of the one time distribution of income from the Toronto Parking Authority (\$20,000) declared in 2008 by the TPA Board but received by the City in 2009;
- adjustment to the parking tag provision which increased revenues (\$4,800);
- draw from Transportation Services Extreme Weather Reserve Fund (\$2,443);
- adjustment to decrease corporate services allowance for doubtful accounts (\$3,750);
- accrual of additional provincial revenues (\$1,435);
- adjustments to ABCs for various reasons including accrual of surpluses (-\$2,553).

Note 2: PSAB adjustments in 2008 are due to:

- adjustment of investments for TCHC and TAF (\$39,781);
- adjustment as a result of TEDCO ceasing to be a GBE (\$72,420);
- accrued vacation pay (\$3,153); and
- adjustment to TCHC deferred revenues (\$1,131)

Financial Condition

The most important measure of any government's financial condition is its net financial asset (liability) position: financial and non-financial assets (cash, receivables, investments, inventory and prepaid expenses) less financial liabilities (trade and employment payables, mortgages and debentures). The City's net liability position at December 31, 2008 (as compared to 2007) increased by \$444 million to \$3.33 billion. This increase in the City's net liability is primarily due to:

- growth in deferred revenue resulting from receipt of funds from the Province as a result of the Investing in Ontario Act, 2008 (\$238 million);
- increase in restricted public transit funds, mainly from Move Ontario 2020 monies received during the year (\$261 million);
- increase in development charge and planning act charge obligatory reserves (\$128 million);
- increase in employee benefit liabilities (\$188 million);
- partially offset by an increase in cash and investments (\$337 million).

The City's long-term debt (Note 10) remained virtually unchanged in the year as debt principal repayments were almost equivalent to new debt issued.

In order to improve the City's net financial liability position, the City continues to implement its Long Term Fiscal Plan. Some key measures included in the plan are: tax policies which enhance economic competitiveness and improve Toronto's business climate, utilization of user rate adjustments for environmental and cost control purposes, creating new revenue sources (land transfer tax and personal vehicle ownership tax, approved by City Council in October 2007 and effective 2008) and working with the Province to realize the upload of social service program costs in 2008 and beyond.

While the debt financing has and will grow due to state of good repair funding requirements and increased focus on improving public transit, the City's updated Capital Plan inclusive of enhanced federal and provincial funding combined with the City's strategic infrastructure partnership reserve fund ensures a solid financing plan is in place for the next five years.

The positive effects of implementing these financial plans are reflected in the City's AA and AA+ independent credit ratings.

Another key indicator of a government's financial condition is the liability amount that must be paid from future revenues (see Note 12 of Consolidated Financial Statements). These liabilities include TCHC mortgages, debentures, employee benefit liabilities, property and liability claim provisions, landfill liabilities and environmental liabilities. In 2008, the total amount that will be recovered from future property taxes and other revenues grew by \$188 million to \$6.45 billion. This increase mainly consists of:

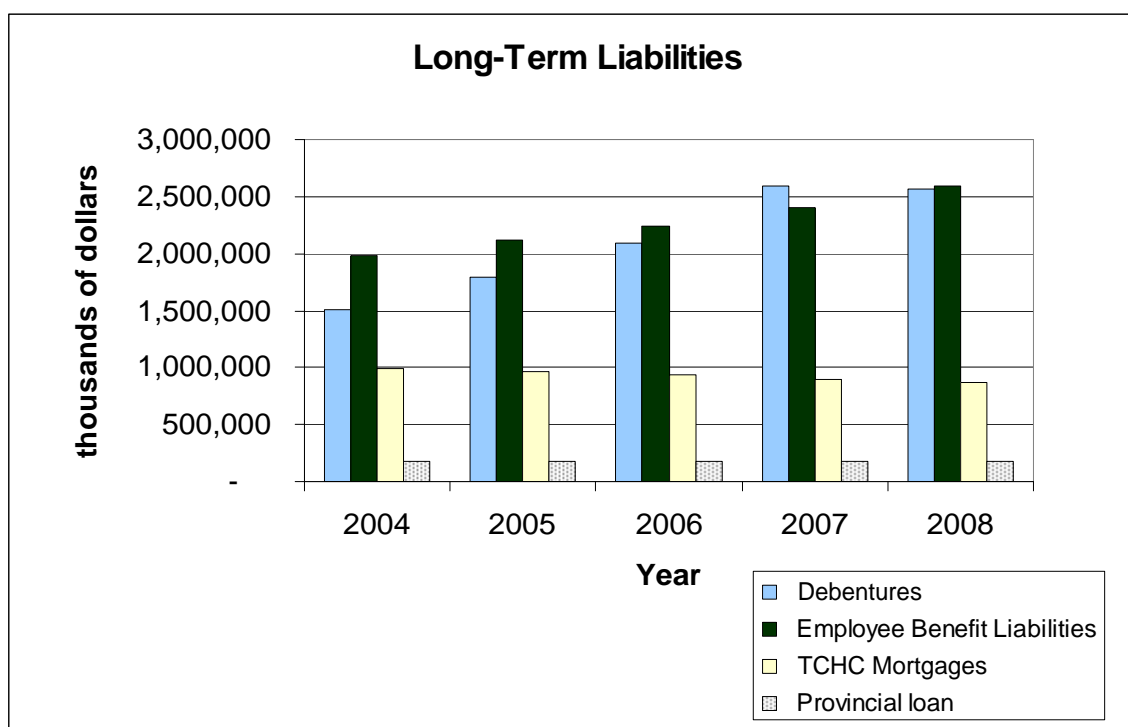
- an increase of \$188 million in employee benefits liabilities;
- an increase of \$32 million in the property and liability claims provision during 2008;
- an increase in landfill closure and post-closure liability of \$11 million;
- offset by decreases in mortgage and long term debt of \$47 million.

Table 1 outlines the trend in financial asset and liability growth over the last 5 years.

Table 1**Net Liabilities – 5 year Summary***(in thousands of dollars)*

Net Financial Liabilities	5 Year Average Annual Increase	2008	2007	2006	2005	2004
Financial Liabilities	9.11%	10,647,259	9,631,062	8,451,699	8,067,913	7,526,205
Financial and Non-financial assets	7.32%	7,312,432	6,739,792	6,166,534	5,825,636	5,514,894
Net Liabilities	13.82%	3,334,827	2,891,270	2,285,165	2,242,277	2,011,311
Percentage Increase		15.34%	26.52%	1.91%	11.48%	

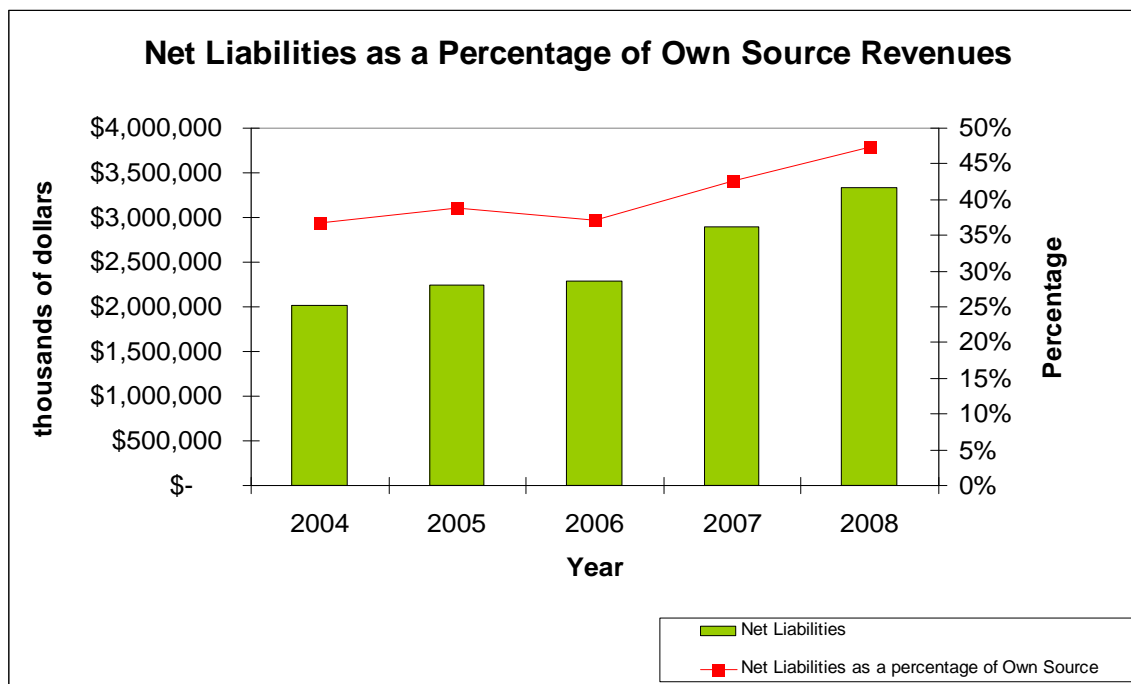
The City's net liabilities have increased by an average annual rate of 13.82% over the last five years attributable to increases in long-term debt to third parties and in long-term employee benefit liabilities. The significant growth in debt has been driven mainly by the need to finance transit capital expenditures and to finance social housing projects as well as the growth of employee benefit liabilities. Chart A provides the breakdown of long-term liability growth by debt type.

Chart A

Additional information on the mortgage liabilities of TCHC can be found in Note 9 of the Consolidated Financial Statements. Note 10 provides additional information about the provincial loan and the City's debenture debt. Further detail about the City's employee benefit liabilities can be found in Note 11 of the Consolidated Financial Statements.

To put the City's net liability into a different context, Chart B expresses the net liability as a percentage of the City's own source revenues (excluding government transfers and earning from investment in government business enterprise (GBE's)). The net liability as a percentage of own source revenues has grown from 36.4% to 47.3% in the last five years.

Chart B

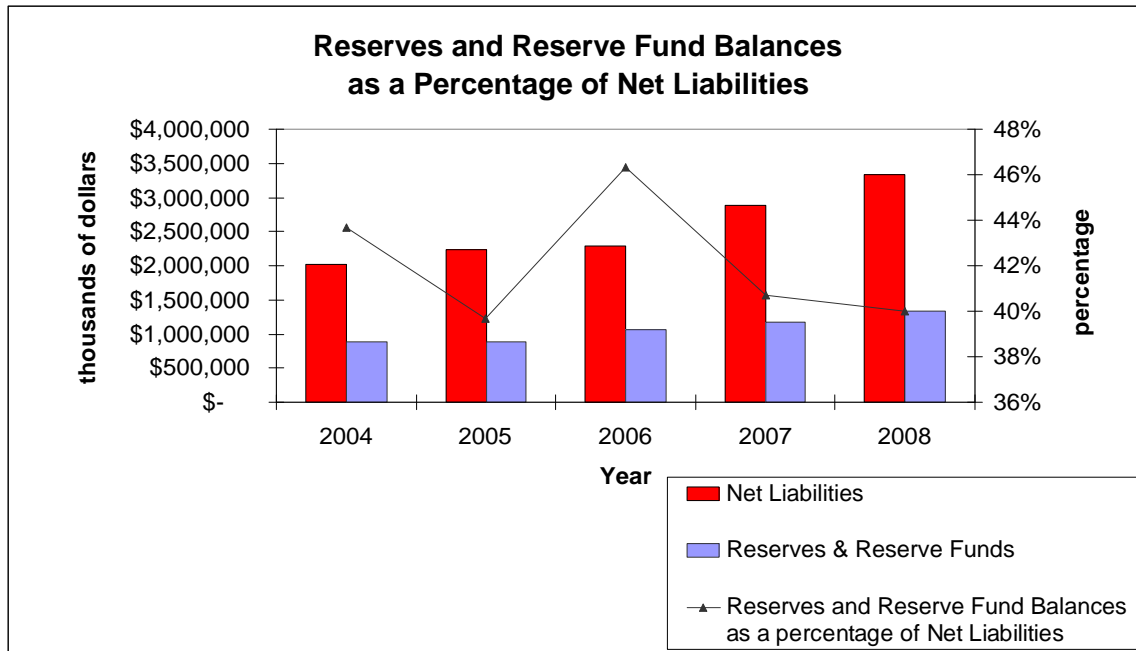


The City's net liabilities substantially exceed the City's reserve and reserve fund balances as shown in Chart C. The vast majority of the reserve and reserve funds are committed to fund capital projects identified in the ten year capital plan, and future known liabilities, leaving only a small portion available for discretionary spending. The balances of all the Obligatory Reserve Funds are restricted for specific purposes as designated by legislation or contractual agreements and all capital reserves/reserve funds are required to replace and maintain capital assets. Also, the current balances of some reserve funds (e.g. Employee Benefits) are not adequate to cover the future obligations for which they have been set aside.

For financial statement purposes, PSAB requires that obligatory reserve fund balances (such as development charges and unspent provincial public transit funding) be classified as deferred revenue (see Note 6 (a) of Consolidated Financial Statements). As a result, the reserve and reserve fund balances in the financial statements are lower than those

included in staff reports to the Budget Committee and Council which include obligatory reserve fund balances.

Chart C



Note 15 of the Consolidated Financial Statements provides a breakdown of the City's reserves and reserve funds.

Comparison to Other Jurisdictions

Table 2 provides a comparison of key financial indicators for a selection of large Canadian cities – 2007 figures.

Table 2

	2007 (in millions of dollars)					
	Toronto	Montreal	Ottawa	Calgary	Edmonton	Vancouver
Investments	3,579	1,236	695	1,819	1,509	806
Investment in GBEs*	1,142	-	297	1,462	2,368	-
Interest bearing long-term debt	3,657	7,600	699	1,697	759	515
Net financial assets (liabilities) (not a total)	(3,051)	(4,746)	(368)	759	2,868	12

* Government Business Enterprises - In other Canadian municipalities as compared above, these types of investments are primarily in electric utility systems and other utility systems such as natural gas and water. Details of Toronto's investments are provided in Note 5 to the Consolidated Financial Statements and include the note receivable from Toronto Hydro Corporation.

The City compares favourably on its investment level. Calgary and Edmonton compare favourably on their net financial position largely because of their government business enterprises and lack of social housing debt.

Analysis of Key Asset and Liability Accounts

Accounts Receivable

Accounts receivable balances increased \$104 million in 2008. The increase consists of: accrual of receivable from the Government of Canada for Federal Gas Tax for 2008 (\$40.7 million); receivable from the Government of Ontario for Ontario Bus Replacement Program (\$25.7 million) and Personal Vehicle Tax (\$3.7 million); accrual of revenue for the new Solid Waste Management Residential Fee Program (\$12.9 million); accrual from York regarding their subway contribution payment (\$10 million); and miscellaneous other increases.

Accounts Receivable	<i>(in thousands of dollars)</i>	
	2008	2007
Government of Canada	178,045	146,088
Government of Ontario	77,452	45,813
Other municipal governments	12,893	1,415
School board	300	600
Water fees	103,920	107,513
Other fees and charges	442,478	409,381
Total	815,088	710,810

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, net of allowance for uncollectible taxes. A breakdown of this receivable is noted below:

Taxes Receivable	<i>(in thousands of dollars)</i>	
	2008	2007
Current year	184,623	158,156
Prior year	26,622	22,780
Previous years	26,942	30,955
Interest/penalty	30,363	30,782
Less: allowance for doubtful accounts	(22,476)	(22,301)
Net receivables	246,074	220,372

Total year end taxes receivable increased by \$25.7 million mainly as a result of the following:

- Economic conditions experienced in 2008 resulted in a \$14.3 million increase in the December 31, 2008 taxes receivable as compared to December 31, 2007. Staff are not concerned about this increase at this time as the amount is fully secured by the underlying property value.
- Year end receivables which are due in future periods increased by \$11.2 million. These receivables include supplementary/omitted levies and other charges issued late in the year and due in the following year, as well as senior deferrals which only become due when property ownership has transferred.

Other Assets

Other Assets increased by \$52.7 million to \$63.9 million (2007: \$11.2 million) due primarily to:

- TCHC advancing an additional \$24.2 million in 2008 to Dundas Parliament Development Corporation (DPDC) for the interim financing of their construction, and
- Consolidation of TEDCO which increased other assets (\$28.5 million) for the following: land held for resale (\$10.5 million), mortgages receivable (\$16.6 million) and other miscellaneous assets (\$1.4 million).

Investments

Investments increased by \$241 million to \$3.82 billion (2007: \$3.58 billion) due primarily to: receipt of funds in 2008 from the Province of \$452 million to fund public transit initiatives and receipt of provincial Investing in Ontario Act funds of \$238 million, offset by debt issuance which was \$415 million less than budgeted. Details about the City's investment portfolios and their yields are provided in Note 3 to the Consolidated Financial Statements.

Investment in government business enterprises

During the year, the City reorganized the activities previously undertaken by TEDCO, with portions transferred to Build Toronto, Invest Toronto and Economic Development, while certain activities remain with TEDCO. As a result of these changes, TEDCO no longer qualifies as a government business enterprise (GBE), and is consolidated as an agency, board or commission (ABC), from the date of incorporation of the two new companies, November 14, 2008. Additional information regarding the City's remaining GBEs as at December 31, 2008 including 2008 transactions for all GBEs with the City as well as condensed financial results, are provided in Note 5 and Appendix 1 to the Consolidated Financial Statements.

Accounts Payable

The breakdown of accounts payable and accrued liabilities at December 31, 2008 with 2007 comparatives is as follows:

Accounts Payable	<i>(in thousands of dollars)</i>	
	2008	2007
Local Board trade payables	465,946	347,138
City trade payables and accruals	770,536	821,201
Payable to school boards	157,376	204,403
Provision for assessment appeals	397,182	373,943
Credit balances on property tax accounts	65,692	107,681
Payroll liabilities	114,086	91,942
Total	1,970,818	1,946,308

Local trade payables were higher in 2008 primarily due to increases in Toronto Transit Commission (TTC) trade payables for \$75.1 million and consolidation of TEDCO payables of \$26.3 million. The provision for tax assessment appeals increased by approximately \$23.2 million given that the total value outstanding with the Assessment Review Board (ARB) increased over the year due to the slow pace of appeals being cleared by the Board. The decrease in credit balances on property tax accounts is due to refunds being issued throughout the year thus reducing the outstanding credit balance. Payroll liabilities were higher as an additional day's pay was accrued in 2008.

Deferred Revenue

Deferred Revenue increased by \$684 million to \$1.92 billion (2007: \$1.24 billion) primarily due to money received in 2008 from the Provincial government for the Investing in Ontario Act - \$238 million and funds for Move Ontario 2020 - \$452 million, the majority of which remained unspent as of December 31, 2008.

Other Liabilities

Other Liabilities increased by \$156 million to \$418.1 million (2007: \$262.3 million), mainly as a result of:

- an increase in the property and liability claims provision (\$31.6 million);
- an increase in the TCHC bank loan (\$43 million);
- increases in Toronto Transit Commission (TTC) in unsettled accident claims (\$20.9 million); and,
- inclusion of TEDCO environmental liabilities (\$47.8 million).

Net Long-Term Debt

Net long-term debt decreased by \$17 million to \$2.74 billion (2007: \$2.76 billion) as follows: issuance of debt totalling \$302 million by the City and Toronto Community Housing Corporation (TCHC), offset by debt repayments and interest earned on sinking funds totalling \$319 million.

Although the City was planning to issue \$200 million in debt in the Fall of 2008, the credit markets froze and capital market conditions deteriorated around mid-September due to the sub-prime mortgage crisis, subsequent bank bailouts and the bankruptcy of

Lehman Brothers in the United States. The decision was made not to issue debt during the remainder of 2008 because the City's cost of borrowing would have increased dramatically. 2009's authority was increased to \$700 million as the debt markets were expected to improve in 2009, which has occurred in recent months.

Employee Benefit Liabilities

Employee Benefit Liabilities increased by \$188 million to \$2.59 billion (2007: \$2.40 billion), as follows:

- increase in the non-OMERS pension plan liabilities (\$78 million);
- increase in sick leave benefits (\$17 million);
- increase in workers' compensation benefits (\$18 million);
- increase in post-employment benefits (\$50 million); and
- change in unamortized actuarial losses (\$25 million).

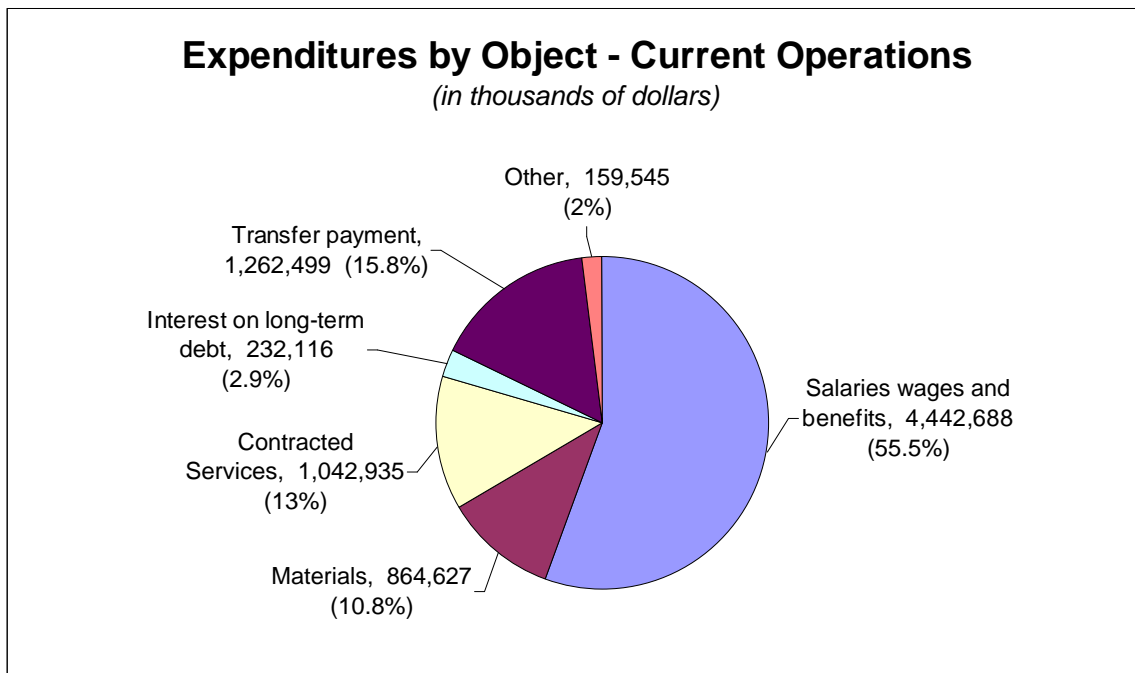
Additional information is provided in Note 11 of the Consolidated Financial Statements.

Operating Expenditures

Gross operating expenditures for 2008 totalled \$8.0 billion (2007: \$7.61 billion). The increase was generated largely by inflationary increases (wages, materials and contracted services), increased employee benefit liabilities and increased interest charges on long-term debt.

Chart D breaks down the gross expenditures by cost object. Salaries, wages and benefits accounted for the largest portion at 55% of the total amount. It should be noted that principal re-payments on debt are not included as they are considered financing transactions for accounting purposes and are not considered expenses.

Chart D



Note 14 to the Consolidated Financial Statements provides a consolidated (operating and capital) summary of expenditures by object.

Table 3 provides a comparison of 2008 actual expenditures by program versus budget, and a comparison with the previous year's actuals.

Table 3

Current Operating Expenditures by Programs

(in thousands of dollars)

Expenditures	2008 Budget	2008 Actual	Difference	Change	2007 Actual
General Government	582,290	666,511	(84,221)	(12.6%)	491,541
Protection to persons and property	1,329,084	1,423,640	(94,556)	(6.6%)	1,426,550
Transportation	1,719,812	1,805,884	(86,072)	(4.8%)	1,656,981
Environmental services	621,481	603,145	18,336	3.0%	593,947
Health services	351,313	368,773	(17,460)	(4.7%)	349,179
Social and family services	1,850,150	1,794,286	55,864	3.1%	1,761,551
Social Housing	608,793	558,895	49,898	8.9%	609,646
Recreational and cultural services	659,201	683,682	(24,481)	(3.6%)	650,896
Planning and development	33,612	99,594	(65,982)	(66.3%)	66,323
Total	7,755,736	8,004,410	(248,674)	(3.2%)	7,606,614

The budget column included in the Consolidated Financial Statements reflects the approved budget at the time the tax levy is approved by Council. Although City Council approves revisions to the budget throughout the year, these amendments are not reflected in the budget column shown in the Consolidated Financial Statements (see Note 17 in the Consolidated Financial Statements).

Table 3 indicates that actual expenditures in 2008 were higher than budget by \$249 million. The primary reason is due to an increase in the PSAB accrual for adjustments for retirement and post employment benefits (\$110.3 million) and an increase in legacy pension plan liabilities (\$77.6 million) due to the immediate recognition of actuarial gains or losses on the City's legacy pension plans which incurred investment losses in 2008. Both of these items are non-cash items that are not included in the City's budget.

In addition to the employee benefit liabilities noted above, a detailed breakdown of contributing factors by function is as follows:

- The General Government category includes an increase in provision for property liability claim provision (\$31.6 million); accruals for tax rebates payable for the new Solid Waste Management Residential Fee Program (\$56.6 million), municipal land transfer tax (\$10.3 million) and personal vehicle tax (\$1.9 million); offset by transfer of the \$75 million special hydro dividend received in operating, prior to transfer to the TCHC State of Good Repair Reserve Fund.

- Actual costs for protection to persons and property (Police, Fire, Building Services and Conservation Authority levies and the Provincial Offences Act Courts) include increased WSIB occupational illness claims (\$7.1 million).
- Transportation includes Roads/Traffic signals maintenance and Transit. The increase resulted from increased snow removal and winter maintenance costs as a result of the large and frequent accumulation of snow. Toronto Transit Commission expenditures were higher than budget primarily as a result of accident claims expenses which were higher than anticipated (\$20 million).
- Environmental services spending was lower than budget due primarily to lower production and efficiencies.
- Health Services increased expenditures included overtime costs due to hospital offloading delays (\$4.4 million).
- Social and Family Services spending was lower than budget by \$55.9 million as average monthly caseload of 75,708 compared favourably to the budgeted caseload of 77,000.
- Social Housing decrease was related to lower than budget spending at TCHC (\$50 million).
- Planning and development spending was higher than budget due to consolidation of Toronto Water Revitalization Corporation (TWRC) (\$11.5 million) and TEDCO (\$46.7 million).

City Revenues

While the annual budget process focuses primarily on property tax increases, it must be emphasized that property taxes are only one of the City's many revenue sources. In 2008, property taxes made up 41.98% (2007 - 41.92%) of the City's operating revenue.

The five year summary of revenues outlined in Table 4 demonstrates that property taxes continue to be the slowest growing revenue source for the City. During this period, assessment growth has been low. In addition, the City has been limited by provincial legislation and Council policy from extending tax rate increases on the commercial, industrial and multi-residential assessment base. The commercial, industrial and multi-residential assessment base represents approximately 58% of the City's tax revenue base.

As a result of the slow growth of property tax revenue, more reliance has been placed on user fees, senior government transfers and other sources of revenue to meet expenditures and minimize property tax rate increases. Council's approval of the Land Transfer and Personal Vehicle Ownership taxes in October of 2007, both of which were implemented in 2008, are examples of the action taken by the City to diversify its revenue sources to address this issue.

Table 4**Consolidated Revenues – 5 year Summary***(in thousands of dollars)*

Revenues	Avg. Annual Increase	2008	2007	2006	2005	2004
Property taxes	3.17%	3,369,949	3,285,947	3,187,263	3,082,009	2,974,975
Municipal land transfer tax (MLTT)	n/a	165,743	-	-	-	-
Personal vehicle Tax (PVT)	n/a	14,992	-	-	-	-
User charges	5.82%	2,108,423	1,966,890	1,856,407	1,766,557	1,681,994
Government transfers	9.49%	2,222,619	1,952,047	2,254,726	1,831,399	1,600,688
Other	14.47%	1,630,979	1,655,652	1,236,089	1,045,713	975,388
Total	7.12%	9,512,705	8,860,536	8,534,485	7,725,678	7,233,045
Percentage Increase		7.36%	3.82%	10.47%	6.81%	-

Increases in property tax revenues averaged 3.17% over the past 5 years. Over the same period, public sector wages increased annually by 3% and non residential construction costs increased by an average of 7.07% annually.

User fees have increased in 2008 due to an increase in Transit Fare passenger revenue (\$56.4 million) as a result of three million additional riders, higher water revenue (\$23.8 million) and additional revenue due to new waste collection fees implemented in 2008 (\$58 million).

Government transfers increase in 2008 is attributable to increased Provincial and Federal Grants for Social and Family Services (\$76.8 million) and increased subsidies for TTC: operating (\$149 million) and capital (\$61 million).

The decrease in other revenue in 2008 as compared to 2007 is attributed primarily to receiving an upfront payment of \$36.5 million from Astral Media in 2007 for the street furniture program.

Table 5 provides a comparison of 2008 revenues by type to budget and Table 6 provides a comparison to previous year.

Table 5

**Current Operating Revenue
Budget to Actual Comparison (2008 Performance)**

Revenue	<i>(in thousands of dollars)</i>			
	2008 Budget	2008 Actual	Difference	Change %
Property Tax revenues	3,315,948	3,369,949	54,001	1.6%
MLTT and PVT	-	180,735	180,735	n/a
User charges	2,132,013	2,108,423	(23,590)	(1.1%)
Government transfers	1,973,170	2,014,261	41,091	2.0%
Other Revenue	759,094	785,381	26,287	3.3%
	8,180,225	8,458,749	278,524	3.3%

The favourable variance in the Property Tax revenues is mainly attributable to the City receiving an additional (fourth) supplementary/omitted assessment roll from MPAC (\$18.8 million), and BIA levies (\$16.9 million).

The unfavourable variance in user charges revenue is mainly attributed to reduced water usage during summer months due to the wet summer (\$19 million). Although water revenues increased in comparison to 2007 due to the rate increase, overall volumes of water decreased during the year.

Table 6

2008 Current Operating Revenue Comparison to Prior Year

Net revenues	<i>(in thousands of dollars)</i>			
	2008 Actual	2007 Actual	Difference	Change %
Property tax revenues	3,369,949	3,285,947	84,002	2.6%
MLTT and PVT	180,735	-	180,735	100.0%
User charges	2,108,423	1,966,890	141,533	7.2%
Government transfers	2,014,261	1,762,325	251,936	14.3%
Other revenues	785,381	824,344	(38,963)	(4.7%)
	8,458,749	7,839,506	619,243	7.9%
Expenditures	8,004,410	7,606,614	397,796	5.2%
Net revenues	454,339	232,892	221,447	95.1%

Property tax revenues increased in 2008 due to the 3.385% tax rate increase on residential property (1.128% increase on commercial & other non-residential property) and a \$26.6 million increase from assessment growth.

Capital Operations

Table 7 provides a comparison of 2008 capital expenditures and financing to budget and Table 8 provides a comparison with the previous year.

Table 7

Capital Operations Budget to Actual Comparisons

(in thousands of dollars)

	2008 Budget	2008 Actual	Difference	Change %
General Government	156,002	99,683	56,319	36.1%
Protection to persons and property	104,905	103,758	1,147	1.1%
Transportation	1,176,412	879,346	297,066	25.3%
Environmental services	479,569	373,210	106,359	22.2%
Health services	11,469	8,370	3,099	27.0%
Social and family services	28,652	15,931	12,721	44.4%
Social Housing	138,467	233,891	(95,424)	(68.9%)
Recreational and cultural services	218,290	157,837	60,453	27.7%
Planning and development	86,193	86,869	(676)	(0.8%)
Expenditures	2,399,959	1,958,895	441,064	18.4%
Revenues	1,262,795	967,108	(295,687)	(23.4%)
Debentures	749,735	308,823	(440,912)	(58.8%)
Operating fund transfers	132,442	180,889	48,447	36.6%
Net reserve/reserve fund transfers	228,560	60,355	(168,205)	(73.6%)
Landfill obligations	-	10,978	10,978	n.a.
Environment Liabilities	-	(25)	(25)	n.a.
Total revenue & financing	2,373,532	1,528,128	845,404	(35.6%)
Net expenditures	26,427	430,767	(404,340)	(1530.0%)

Gross capital expenditure levels continue to be under budget. This is primarily attributed to: the inability to find or secure suitable sites in accordance with planned timeframes; the need to revise design plans; delays in securing funds from cost-sharing partners; unanticipated delays in construction start-up and deferral of work; unanticipated legal and environmental issues; challenges in hiring qualified staff; and delays in the delivery of equipment from manufacturers. In addition, several projects were completed under-budget.

Transportation Services' lower than budget spending occurred mainly in the Program's major projects which require third party coordination and included the following:

- The *St. Clair Dedicated Right of Way* project which was under spent due to longer than anticipated utility work with Toronto Hydro and Toronto Water.
- The *Bloor Street Transformation* Project was delayed by a court challenge and scheduling adjustments arising from the need to accommodate the local BIA's expressed intent to minimize disruptions to their seasonal shopping period during the latter part of 2008.

- The *Dufferin Jog Elimination* project experienced construction delays resulting from design changes and coordination obstacles with railways.

Toronto Transit Commission (TTC) lower than budget spending was mainly attributable to the following:

- Decreased project spending on Wheel-Trans due to difficulty in finding a manufacturer who is capable of producing a paratransit vehicle suitable to Wheel Trans' needs (\$17.4 million).
- Surface track work deferral of work on the St. Clair Reserved Transit Line and deferral of associated track work on St. Clair (\$37.1 million).
- Replacement of 40 foot diesel/electric hybrid buses is behind schedule due to a strike at the bus manufacturer in 2007 resulting (\$30.5 million).
- Spadina Subway Extension project deferral of engineering work and property acquisition to 2009 (\$46.5 million).
- Purchase of streetcars delayed due to timing of the project (\$54 million)

Table 8

**Capital Expenditures by Program
with Previous Year Comparison and Percentage Change**

(in thousands of dollars)

Expenditures by Programs	2008	2007	Difference	Change %
General Government	99,683	88,957	10,726	12.1%
Protection to persons and property	103,758	74,000	29,758	40.2%
Transportation	879,346	741,910	137,436	18.5%
Environmental services	373,210	466,105	(92,895)	(19.9%)
Health services	8,370	6,950	1,420	20.4%
Social and family services	15,931	19,924	(3,993)	(20.0%)
Social Housing	233,891	194,138	39,753	20.5%
Recreational and cultural services	157,837	198,105	(40,268)	(20.3%)
Planning and development	86,869	69,856	17,013	24.4%
Total	1,958,895	1,859,945	98,950	5.3%

Although capital spending has remained under budget, actual spending increased significantly over the previous year for a majority of the programs in line with Council's direction to increase the level of capital completion rates. This included increased spending in 2008 in Toronto Water as a result of construction proceeding on several large projects (\$65 million) offset by a decrease in Solid Waste (as the Green Lane landfill was purchased in 2007); increased spending in TTC due to delivery of additional diesel buses in 2008 and increased spending in TCHC for their social housing projects.

Segmented Reporting

Public Sector Accounting standard 2700 Segmented Disclosures came into effect for the 2008 reporting year. The purpose of the standard is to provide information about segments to:

- help users of the financial statements identify the resources allocated to support the major activities of the government;
- help users of the financial statements make more informed judgments about the government reporting entity and about its major activities;
- help users of financial statements better understand the manner in which the organizations in government are organized and how the government discharges its accountability obligations;
- enhance the transparency of financial reporting; and
- help users of the financial statements better understand the performance of the segments and the government reporting entity.

Although the standard does not prescribe which segments to report, the current year reporting has been based on reviews of other municipalities' reported segments and discussions with other municipal treasurers. For this first year, segmented reporting is provided for the functional spending areas (Appendix 2), entities (Appendix 3), as well as functional areas with comparisons to budget (Appendix 4). It is anticipated that the segmented information reported will change over time, and will include service level information, once the City has adopted a service level budget.

Risks and Mitigates

The City continues to face a number of risks that could have a negative impact on the City's financial future. These risks include: lack of long-term dedicated funding to assist the City in addressing its infrastructure deficit including building and expanding the transit system to meet the City's strategic goals and accessing non-property tax revenue sources that grow with the economy to ensure long term sustainable funding.

In 2008, the City made significant progress to address these risks by continuing to implement its Long Term Financial Plan. Appendix B lists eight (8) specific financial issues/risks and the actions taken in 2008 to address them.

Highlights include: diversifying the City's revenue sources and generating additional revenue from the Municipal Land Transfer Tax (MLTT) and Personal Vehicle Ownership Tax (PVT), approving a long-term plan to reduce unfunded liabilities, continuing tax policies which enhance economic competitiveness, continuing cost containment initiatives, and continuing to work with the Province to realize the upload of the social service programs.

Evaluating the City's Performance

The financial statements and the credit ratings do not provide an assessment of value for money. The City examines its performance internally and externally, relative to other municipalities, and performance measures are an integral part of the budget preparation and review process.

Toronto's performance continues to compare favourably against other Ontario municipalities in a number of areas based on the measures reported under the provincially mandated Municipal Performance Measurement Program (MPMP) and the Ontario Municipal CAO's Benchmarking Initiative (OMBI).

A detailed report entitled "Toronto's 2007 Performance Measurement and Benchmarking Report" was presented to the Executive Committee on April 7, 2009 and compares Toronto's 2007 results in 23 different service areas to those of 14 other Ontario municipalities in the performance categories of service level, efficiency, customer service and community impact.

The report also includes a summary of the City's internal trends between 2006 and 2007. For 88% of the service level indicators, Toronto's service levels had been maintained or increased in 2007. For performance measures relating to efficiency, customer service and community impact, 66 % of the measures either improved or remained stable in 2007.

The full report entitled Toronto's 2007 Performance Measurement and Benchmarking Report can be found on the City's website at http://www.toronto.ca/city_performance/pdf/consolidated-2007-PMBR-report.pdf

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ATTACHMENTS

Appendix A: 2008 Consolidated Financial Statements

Appendix B: Key Issues/Risks Facing the City of Toronto

Appendix C: Five Year Summary of Consolidated Revenues and Expenditures