



Sinking Funds – 2019 Audited Financial Statements

Date: November 2, 2020

To: Audit Committee

From: Controller

Wards: All

SUMMARY

The City of Toronto (City) maintains portfolios of sinking funds in order to build up funds used to repay City debt when it matures. Sinking fund contributions are invested; the investment earnings help reduce the amount of City own-source cash used to repay amounts borrowed. Sinking funds form part of the City's consolidated cash balances.

This report presents the City's Sinking Funds Audited Financial Statements for the year ended December 31, 2019 and provides highlights of the Sinking Funds' 2019 financial performance as of December 31, 2019.

The Sinking Funds Audited Financial Statements have been prepared by management who is responsible for ensuring that proper internal controls have been applied to the presentations in each statement. The City's 2019 auditors, PricewaterhouseCoopers LLP (PwC), are responsible for providing an opinion on the fair presentation of the financial statements in accordance with Public Sector Accounting Standards (PSAS). The Audit Committee is responsible for approving the statements prior to City Council approval. The 2019 Sinking Funds Financial Statements received an unqualified audit opinion from PwC. In addition, there are no internal control recommendations related to the 2019 Sinking Fund Audited Financial Statements.

Financial statements and auditor's reports are typically reported to the Audit Committee and Council in June, when external audit work is substantially complete. During the external auditor's normal engagement period, management's focus was on the COVID-19 response and meeting operational requirements. Additionally, public health restrictions put in place because of the pandemic required that the audit process be conducted in an extended fashion over a longer period of time. As a result, the completion of the 2019 financial statements and external audit was delayed.

RECOMMENDATIONS

The Controller recommends that:

1. City Council approve the 2019 Audited Financial Statements for the City of Toronto Sinking Funds as attached in Appendix A to this report.

FINANCIAL IMPACT

There is no financial impact resulting from the adoption of the recommendation in this report.

The Chief Financial Officer and Treasurer has reviewed this report and agrees with the financial impact information.

DECISION HISTORY

On an annual basis, the City presents the audited financial statements of the City's Sinking Funds to the Audit Committee and Council for approval.

Below is a link to the staff report for the 2018 audited financial statements for the City's Sinking Funds:

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2019.AU3.9>

COMMENTS

When the City issues debentures (debt), the City of Toronto Act, 2006 requires that the principal repayment be amortized over the term-to-maturity of the debenture or that an annual amount be contributed to a Sinking Fund. When a sinking fund is established, the annual contribution and the investment earnings on those contributions accumulate to repay City debt when it matures. The City follows its Council approved investment policy when investing sinking fund contributions.

The 2019 weighted average rate of return for Sinking Fund investments was 4.86% (2018 – 3.21%).

Currently, the City has five (5) separate sinking fund portfolios supporting thirty one (31) individual debenture issues at varying stages of maturity. Sinking fund assets as at December 31, 2019 amounted to \$1.6 billion. These assets represent amounts held to discharge City debt of \$7.1 billion (2018 - \$6.5 billion) maturing between 2021 and 2049.

The accompanying Sinking Funds Financial Statements are prepared in accordance with Public Sector Accounting Standards, except for investments which are recorded at fair value to better reflect their ability to meet debt retirement obligations. Preparation of the financial statements is the responsibility of City management, who are required to ensure that proper internal controls are applied to ensure fair presentation.

Statement of Financial Position

The Sinking Funds Statement of Financial Position outlines the assets and liabilities of the fund, representing the financial position at the end of the stated fiscal year.

Total Current Assets of \$1.6 billion are comprised of cash holdings and investments made with contributions to the sinking funds. These balances vary depending on debt repayment, cash injections and investment decisions. Investments are recorded at fair value.

Total Current Liabilities consist mainly of the actuarial requirements of the sinking fund to reach the required debt repayment value at maturity. The actuarial requirements liability at December 31, 2019 amounted to \$1.6 billion, a decrease of \$6 million from the prior year end balance.

Net Assets are comprised of two amounts, unrestricted surplus and internally restricted surplus. The unrestricted surplus results from the fund earning amounts greater than the actuarial rate of return that was assigned to a debenture when it was issued. These funds are available to address shortfalls in earnings in future years or could be redirected by the Chief Financial Officer and Treasurer.

In 2010, a \$600 million contribution was made to the sinking funds, which created the internally restricted surplus. This contribution has been drawn down and recognized as part of annual income through the enactment of specific debenture by-laws in order to help with maturity obligations, which has helped to reduce the City's overall liabilities.

The unrestricted surplus increased during the year by \$5.4 million, as a result of an increase in 2019 fund revenues over 2019 expenses of \$5.4 million. The increase is mainly due to the difference between of actuarial requirements and actual earnings.

Statement of Operations and Changes in Unrestricted Surplus

The Statement of Operations shows the annual revenues and expenses of the sinking fund and reports the annual surplus or deficit from the financial activity during the stated fiscal year. The total surplus reconciles to the unrestricted and internally restricted total on the Statement of Financial Position.

Annually, there are two sources of revenue for sinking funds – contributions, which represent the cash contributions made by the City to support actuarial requirements for future debt repayment and investment earnings, which represent income from investing sinking fund balances. Revenues for 2019 increased by \$80 million to \$399.9 million (2018 - \$319.9 million), due to an increase in investment income of \$56 million and an increase in contributions into the Sinking funds of \$24 million.

The 2019 increase in investment income of \$56 million is attributable to two factors: a \$21 million increase in unrealized gain from the change in debenture market value and an average rate of return which was 3.23% higher in 2019 than 2018.

When the balance required to meet the debt liability maturity requirements, increases, the amount is expensed in the Statement of Operations. The \$394.4 million (2018 - \$383.1 million) expense in 2019 represents the 2019 increase in the liability amount.

Statement of Cash Flows

The statement of cash flows reports the changes in the cash balance throughout the year, with cash being used to support investing and financing activities, and to fund operations.

Audit Results

The Sinking Funds financial statements are audited by PricewaterhouseCoopers (PwC), who is responsible for applying sufficient and adequate audit testing in order to provide an opinion on the fair presentation of the financial statements.

In performing their work, PwC may recommend adjustments to the balances, or can comment on process or internal control improvement.

For the 2019 Sinking Funds financial statements, no recommendations were made.

The PwC 2019 Year End report to the Audit Committee is presented with the financial statements.

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SIGNATURE

Andrew Flynn
Controller

ATTACHMENTS

Appendix A: 2019 Sinking Funds Financial Statements
Appendix B: 2019 Year-End Report to the Audit Committee