

2019 Sinking Funds Financial Statements

December 31, 2019

Independent Auditor's Report

PriceWaterhouseCoopers (PwC) signed and dated opinion to be inserted following City Council approval

CITY OF TORONTO SINKING FUNDS
STATEMENT OF FINANCIAL POSITION

as at December 31, 2019 (in thousands of dollars)

	2019	2018
ASSETS		
Current		
Cash	499,935	268,449
Investments (Note 4)	1,137,522	1,369,148
Total Current Assets	1,637,457	1,637,597
LIABILITIES AND NET ASSETS		
Current		
Accounts Payable and Accrued Liabilities	3	11
Total Current Liabilities	3	11
Actuarial Requirements (Note 5)	1,556,839	1,562,398
Total Liabilities	1,556,842	1,562,409
Net Assets		
Unrestricted Surplus (Note 6)	80,615	20,585
Internally Restricted Surplus (Note 6)	-	54,603
Total Surplus	80,615	75,188
	1,637,457	1,637,597

The accompanying Notes and Appendices are an integral part of these Financial Statements.

CITY OF TORONTO SINKING FUNDS
STATEMENT OF OPERATIONS AND CHANGES IN UNRESTRICTED SURPLUS

for the year ended December 31, 2019 (in thousands of dollars)

	2019	2018
REVENUES		
Contributions	315,499	291,463
Investment Income (Note 7)	84,369	28,444
Total Revenue	399,868	319,907
EXPENSES		
Changes in Actuarial Requirements (Note 5)	394,441	383,115
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES FOR THE YEAR	5,427	(63,208)
SURPLUS – BEGINNING OF YEAR	75,188	138,396
TOTAL SURPLUS – END OF YEAR	80,615	75,188

The accompanying Notes and Appendices are an integral part of these Financial Statements.

CITY OF TORONTO SINKING FUNDS
STATEMENT OF CASH FLOWS

for the year ended December 31, 2019 (in thousands of dollars)

CASH PROVIDED BY (USED IN)	2019	2018
OPERATING ACTIVITIES		
Excess (deficiency) of revenues over expenses for the year	5,427	(63,208)
<i>Add (deduct) items not involving cash:</i>		
Amortized discount on investments	(18,661)	(34,767)
Increase in accrued interest	(1,583)	53
Decrease in unrealized gain on investments	3,717	24,895
Increase in actuarial requirements	394,441	383,115
 <i>Changes in non-cash working capital balances related to operations:</i>		
(Decrease) in accounts payable and accrued liabilities	(8)	(5)
Cash provided by operating activities	383,333	310,083
INVESTING ACTIVITIES		
Purchase of investments	(959,295)	(856)
Proceeds from maturities of investments	816,862	377,773
Proceeds from sale of investments	390,586	4,818
Cash provided by investing activities	248,153	381,735
FINANCING ACTIVITIES		
Maturity of debenture	(400,000)	(425,000)
Cash used in financing activities	(400,000)	(425,000)
 Increase in cash during the year	 231,486	 266,818
Cash, beginning of year	268,449	1,631
Cash, end of year	499,935	268,449

The accompanying Notes and Appendices are an integral part of these Financial Statements.

CITY OF TORONTO SINKING FUNDS

NOTES TO THE FINANCIAL STATEMENTS

December 31, 2019 (in thousands of dollars)

1. Purpose of Sinking Funds

The City of Toronto Sinking Funds [the Sinking Funds] accumulate amounts through periodic contributions, which are calculated such that the contributions and interest earnings will be sufficient to retire the principal amount of the Sinking Fund debt when it matures. When the accumulated Sinking Fund exceeds the maturity value of the related debenture, the excess may be refunded or applied against other Sinking Fund accounts created for the same purpose.

Note 8 in these financial statements contains the schedule of projected debenture maturity amounts.

The City of Toronto Sinking Funds are governed under the City of Toronto Act, 2006 and are exempt from income taxes under Section 149(1) of the Income Tax Act (Canada).

2. Summary of Significant Accounting Policies

These financial statements have been prepared in accordance with Canadian public sector accounting standards, except that investments are recorded at fair value to better reflect their ability to meet debt obligations. The significant accounting policies are summarized below.

(i) Financial instruments

The Sinking Funds financial assets include cash, short-term and long-term investments. Cash is recorded at amortized cost, which approximates fair value. Short term investments are comprised of money market instruments, such as guaranteed investment certificates and are valued based on cost plus accrued investment/interest income. The Sinking Funds invest in debentures issued or guaranteed by Provincial and Municipal governments and corporate bonds; the fair value of investments recorded in the financial statements is based on the latest bid prices and the change in fair value is included in the Statement of Operations as Investment Income. Investment transactions are recorded on a settlement date basis and transaction costs are expensed as incurred.

The Sinking Funds' investment activities expose it to a range of financial risks, including market risk, credit risk, and liquidity risk (Note 9).

(ii) Revenue recognition

Contributions are recognized as revenue in the year receivable. Interest income is recorded when earned.

Sinking Fund debenture issues are grouped by Sinking Fund interest rates. These rates represent the investment earnings assumptions for each of the respective funds and are used in determining the annual contributions required to retire the outstanding debt.

Investment income includes investment income and interest income, net of bank service charges, audit fees and unrealized gain (loss) on the increase/decrease in the fair value of the investments.

3. Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amount of assets, liabilities and deficit/surplus at the reporting date and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimates. In particular, there is significant judgement applied in determining actuarial requirements for Sinking Funds.

CITY OF TORONTO SINKING FUNDS
NOTES TO THE FINANCIAL STATEMENTS

December 31, 2019 (in thousands of dollars)

The Actuarial Requirements Liability of the Sinking Funds for the year represents the amounts levied during the year as set out in the Sinking Funds debenture bylaws plus interest accrued, compounded at the Sinking Fund rates of 3.5%, 4%, or 5% per annum on debt issued in 1997 and after; and 2.0%, and 2.5% per annum on debt issued in 2015 and after. These actuarial requirement liabilities are presented at amortized cost, which approximates fair value.

4. Investments

Fair value represents bid price for each financial instrument, while face value represents the original cost of the investment at the purchase date. Sinking Fund investments will be held to maturity, and no write-down to market value is required given that the fair value of the investments is lower than the face value of the investments.

	Fair value	Face value
2019		
Debt investments issued or guaranteed by:		
Provincial Governments	589,046	807,441
City of Toronto	25,860	22,278
Other Canadian municipalities	82,633	73,081
Corporations	315,806	297,006
Total Debt	1,013,345	1,199,806
Equity investments issued or guaranteed by:		
Corporations	<u>124,177</u>	<u>12,182</u>
Total Equities	<u>124,177</u>	<u>12,182</u>
Total Equity	1,137,522	1,211,988
2018		
Debt investments issued or guaranteed by:		
Provincial Governments	1,027,182	1,198,513
City of Toronto	93,574	86,397
Other Canadian municipalities	216,754	198,867
Corporations	31,638	31,769
Total	1,369,148	1,515,546

	2019	2018
Amortized cost	1,111,300	1,339,209
Weighted average rate of return	4.86%	3.21%
Average term to maturity	15.67 years	6.38 years
Excess of fair value over amortized cost	26,222	32,549

CITY OF TORONTO SINKING FUNDS
NOTES TO THE FINANCIAL STATEMENTS

December 31, 2019 (in thousands of dollars)

5. Actuarial Requirements

	2019	2018
Actuarial Requirements, beginning of year	1,562,398	1,604,283
Add change in Actuarial liability requirements	394,441	383,115
	1,956,839	1,987,398
Less value of debentures matured during the year	400,000	425,000
Actuarial Requirements, end of year	1,556,839	1,562,398

6. Net Assets

	2019	2018
City of Toronto unrestricted surplus based on amortized cost	54,393	(9,354)
Unrealized gain on investments	26,222	29,939
Total unrestricted surplus	80,615	20,585
Internally restricted surplus	-	54,603
Total net assets	80,615	75,188

7. Investment Income

	2019	2018
Investment income	76,315	50,886
Interest income	11,771	2,453
Unrealized loss on change in fair value	(3,717)	(24,895)
Total investment income	84,369	28,444

8. Schedule of Projected Debenture Maturities

For the year ended December 31, 2019, the following is a list of the projected maturities of the Sinking Fund debentures, held within the City of Toronto. The list only includes references to years in which a maturity of a debenture is projected to occur.

	2019
2021	650,000
2023	300,000
2024	300,000
2025	300,000
2026	300,000
2027	700,000
2029	400,000
2035	400,000
2036	750,000
2039	200,000
2040	600,000
2041	450,000

CITY OF TORONTO SINKING FUNDS
NOTES TO THE FINANCIAL STATEMENTS

December 31, 2019 (in thousands of dollars)

	2019
2042	300,000
2044	300,000
2046	500,000
2048	300,000
2049	350,000
	<u>7,100,000</u>

9. RISK EXPOSURE

The Sinking Funds are subject to market risk, credit risk, and interest rate risk with respect to the investment portfolio. The Sinking Funds' interest bearing investments are exposed to interest rate risk. Sinking Funds' investments are at risk due to fluctuations in market prices whether changes are caused by factors specific to the individual investment or factors affecting all securities traded in the market. The Sinking Funds manage risk by investing across a wide variety of asset classes and investment strategies.

The Sinking Funds hold investments in fixed income securities issued by corporations and government entities and as such have fixed income credit risk. The Sinking Funds mitigate this risk by limiting the investment portfolio to investments in BBB grade or higher.

The Sinking Funds' liquidity risk is the risk of being unable to settle or meet commitments as they come due. These commitments include payment of the funding obligations of the Sinking Funds. Liquidity risk is managed by ensuring the Sinking Funds invest in securities that are actively traded.

With the creation of the City's Investment Board and new investment policy as at January 1, 2018, through provincial regulation 610/06, sinking fund contributions can be invested in a broader range of asset classes including fixed income, equities and real assets.

10. CAPITAL MANAGEMENT

In managing capital, the Sinking Funds focus on liquid resources available for reinvestment. The Sinking Funds' objective is to have sufficient liquid resources to meet its debenture obligations when they mature. The need for sufficient liquid resources is considered in the investment process. As at December 31, 2019, the Sinking Funds have met their objective of having sufficient liquid resources to meet current obligations.

11. SUBSEQUENT EVENTS

On March 11, 2020, the World Health Organization characterized the outbreak of a strain of the novel coronavirus (COVID-19) as a pandemic which has resulted in a series of public health and emergency measures that have been put in place to combat the spread of the virus. On March 23, 2020, the City declared a state of emergency. These public health and emergency measures, which include the implementation of travel bans, self-imposed quarantine period and social distancing, have caused material disruption to businesses globally resulting in an economic slowdown. The impact of COVID-19 pandemic is considered to be a non-adjusting event at the balance sheet date and accordingly, the City has not reflected these subsequent conditions in the measurement of its assets as at December 31, 2019.

Given the ongoing and dynamic nature of the circumstances surrounding COVID-19, it is difficult to predict how significant the impact of COVID-19, including any responses to it, will be on the economy and the City's operations in particular, or for how long any disruptions are likely to continue. The extent of such impact will depend on future developments, which are highly uncertain, rapidly evolving and difficult to predict, including

new information which may emerge concerning the severity of COVID-19 and additional actions which may be taken to contain COVID-19, as well as the timing of the re-opening of the economy in Canada.

In response to the City's efforts in addressing COVID-19, the organization has experienced decreases to its revenues and increases to its expenditures.