

2021 Audited Financial Statements - Consolidated City, Sinking Funds, and Consolidated Trust Funds

Date: June 24, 2022

To: Audit Committee

From: Chief Financial Officer and Treasurer and Controller

Wards: All

SUMMARY

This report presents the City of Toronto's (City) Audited Consolidated Financial Statements (Consolidated Statements), the Audited Sinking Fund Financial Statements (SF Statements) and the Consolidated Trust Funds Financial Statements (TF Statements) for the year ended December 31, 2021, for approval, to the Audit Committee and City Council.

The report provides highlights of financial performance and financial condition as at December 31, 2021. All City financial statements are prepared in accordance with Public Sector Accounting Standards (PSAS) established by the Public Sector Accounting Board (PSAB) of the Chartered Professional Accountants (CPA) of Canada.

The Consolidated Statements include all City divisions and entities within the City's control; a full list is included in Note 1 accompanying the Consolidated Statements. Highlights of 2021's financial results are as follows:

- **Statement of Financial Position:** the City recognized financial assets of \$14.9 billion, liabilities of \$23.3 billion, net debt of \$8.4 billion, and non-financial assets, comprised mainly of the City's tangible capital assets used to support the delivery of City services, of \$38.8 billion.
 - Although the City's net debt decreased by \$0.2 billion, the balance of \$8.4 billion continues to signify that the City will need to identify future sources of revenue to settle its liabilities given that the City does not currently have sufficient financial assets to settle anticipated expenditures in future fiscal periods; and
- **Statement of Operations:** the City recognized revenues of \$15.2 billion, which included \$1.8 billion of government grants provided by senior levels of government, such as those provided under the Safe Restart arrangement and the Province of Ontario's vaccination program, to support the City's pandemic efforts, in addition to supportive housing and refugee costs. . The City also incurred expenses of

\$13.2 billion, which reflects costs incurred in 2021 to provide critical frontline services to residents and businesses within public health guidelines.

Consistent with other Canadian municipalities, the City is legislatively required to have a balanced budget and therefore, is prohibited to budget for a deficit. In order to comply with these legislative requirements, the City uses a cash basis of accounting for budgeting purposes; however, the Consolidated Statements are prepared and presented using an accrual basis of accounting, which is required under PSAS. As the City uses a different methodology to prepare the budget versus the financial statements, financial statement users may note that the way in which the City calculates its budget in each of these financial documents is different. As a result, the City includes a separate reconciliation to illustrate key differences in accounting principles, such as the recognition of tangible capital assets and associated amortization costs on the Consolidated Statements, and explains why an accounting surplus is recognized. In the Consolidated Statements, the City recognized an accounting surplus of \$2.0 billion in the current year.

The Sinking Funds, which form part of the City's consolidated cash balances, are a significant financial resource for the City, especially as these assets are ultimately used to discharge the City's debt in accordance with the timing of when its loans mature. The Sinking Funds are accumulated and invested throughout the year and reduce the City's reliance on its own-source cash when making its debt repayments.

The Trust Funds are assets benefiting the City and its Agencies and Corporations, mainly held in cash and investments and administered through the City and the Toronto Police Services Board. Although these trust funds are assets to the City and its consolidated entities, they represent liabilities to third parties and therefore, are not included in the City's Consolidated Statements.

The City's management team is responsible for preparing the Consolidated Statements (Appendix A), SF Statements (Appendix B), and the TF Statements (Appendices C and D) in accordance with PSAS, as well as ensuring that appropriate internal controls are in place to safeguard the City's assets and financial information.

The City's external auditors, KPMG LLP (KPMG), are responsible for providing an opinion on the fair presentation of the above financial statements in accordance with PSAS. KPMG executes audit procedures in order to gather sufficient and appropriate audit evidence with which to form an opinion on the City's financial statements. In performing their work, KPMG may recommend adjustments to the City's balances or note disclosures included in its financial statements, or improvements to management's internal processes and internal controls. KPMG's Year End 2021 Audit Findings Report comprises a separate submission to the Audit Committee. KPMG has issued an unqualified audit opinion on the City's 2021 Consolidated Statements, SF Statements, and TF Statements.

The Audit Committee is responsible for approving the financial statements prior to City Council's approval.

RECOMMENDATIONS

The Chief Financial Officer and Treasurer and the Controller recommend that:

1. City Council approve the 2021 Audited Consolidated Financial Statements in Appendix A to this report.
2. City Council approve the 2021 Audited Sinking Fund Financial Statements in Appendix B to this report.
3. City Council approve the transfer of the surplus cash balance of \$14 million in response to the maturity of the 5% sinking fund to the active 3.5% sinking fund.
4. City Council authorize the Chief Financial Officer and Treasurer, or designate, to reallocate surplus cash resulting from the closure of any sinking funds after the debt for which the sinking fund was established has been fully paid, to another active sinking fund.
5. City Council approve the 2021 Audited Consolidated Trust Funds Financial Statements in Appendix C to this report.

FINANCIAL IMPACT

The last debenture, to be settled from the 5% sinking fund, matured in 2021, the remaining sinking fund balance is 29.6 million. To strengthen the City's ability to finance repayments in the future, it is recommended that these surplus funds be transferred to the 3.5% sinking fund. Maintaining these funds in sinking funds will mitigate future pressures on debt servicing costs.

Total audit fees of \$477,000 for the financial statement audits were approved in the 2021 budget. There are no financial implications resulting from the approval of the 2021 audited financial statements recommended in this report.

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

DECISION HISTORY

As required by Sections 231 and 232 of the City of Toronto Act, 2006 (Act), the City prepares and publishes annual financial statements that consolidate the financial results of all entities that the City controls. A list of these entities is provided in Note 1 of the Statements.

Section 231 of the Act requires that the financial statements be prepared in accordance with generally accepted accounting principles (GAAP) established by the Chartered Professional Accountants of Canada's Public Sector Accounting Board (PSAB).

Below is a link to the staff report for the 2020 Audited Consolidated Financial Statements, 2020 Audited Sinking Fund Financial Statements, and 2020 Audited Consolidated Trust Fund Financial Statements for the City of Toronto:

<https://www.toronto.ca/legdocs/mmis/2021/au/bgrd/backgroundfile-168605.pdf>

COMMENTS

Responsibility for the City's Consolidated Statements, SF Statements and TF Statements

On an annual basis, the City prepares its financial statements in accordance with PSAS. This key financial reporting activity allows the City's internal and external stakeholders to understand the City's financial position and performance. For purposes of providing additional context, the City publishes its financial statements, as well as additional information concerning its finances, operations, and climate-related matters in the Annual Financial Report, linked here: [Annual Financial Report](#)

The preparation, content and accuracy of the City's financial statements and all other information included in the Annual Financial Report is the responsibility of management, as outlined in PSAB's financial reporting framework. Management is responsible for ensuring that proper internal controls are developed, maintained, and applied to ensure fair presentation of the financial statements. In addition, management must record and report transactions in accordance with PSAS to ensure that its overall financial information has been fairly represented.

The City's Consolidated Statements, SF Statements and TF Statements have been reviewed and approved by the Chief Financial Officer and Treasurer and the Controller, as well as audited by the City's external auditors, KPMG LLP.

The City's Consolidated Statements: Major Components

The Consolidated Statements consist of four major components:

- Statement of Financial Position: provides an overview of key financial balances, including what the City owns (e.g. investments and tangible capital assets) and owes to others (e.g. accounts payable and long-term debt) as at December 31st;
- Statement of Operations and Accumulated Surplus: outlines the current year's revenues, expenses, and accounting surplus for the City's Divisions and its consolidated entities;
- Statement of Change in Net Debt: outlines how changes in the City's non-financial assets, including tangible capital assets, affected the net debt balance. This is an important financial statement, especially as net debt represents the future revenue required to pay for its obligations arising from past transactions and services provided by the City to residents and businesses; and
- Statement of Cash Flows: summarizes the City's cash position and changes resulting from the various sources and uses of cash.

Based on PSAS' financial reporting requirements, the Consolidated Statements are presented on an accrual accounting basis, which allows the City to disclose the long-term financial implications associated with its activities and decisions. As a result, the Consolidated Statements incorporate principles that differ from those that the City applies when preparing its annual budget. For example, recognition on the Statement of Operations is dependent on when revenues are earned and when expenditures are incurred, irrespective of when cash is formally received or used to settle existing obligations. In addition, PSAS provides standards for the recognition of assets and liabilities in the Statement of Financial Position; this recognition may differ from how

financial transactions are treated using the modified cash basis of budgeting, such as the recognition of Tangible Capital Assets as non-financial assets or the recognition of Long Term Debt as a liability requiring future repayment.

The City's Consolidated Statements: Financial Highlights

In 2021, the City's overall financial results remained relatively consistent with the patterns identified in the previous year due to the City's continued efforts responding to the pandemic.

Financial highlights of 2021 are as follows:

(in millions of dollars)

Line item	2021	2020	Change (\$)	Change (%)
Financial assets	14,941	14,113	828	6
Liabilities	23,320	22,718	602	3
Net debt	8,379	8,605	(226)	(3)
Non-financial assets	38,805	37,033	1,772	5
Revenues	15,241	14,075	1,166	8
Expenses	13,243	12,453	790	6
Annual surplus	1,998	1,622	376	23

Financial assets increased mainly as a result of the growth of the City's cash and cash equivalents balance, which reflected the City's ability to resume its collection of outstanding accounts and taxes receivables, the accumulation of development charges to be used towards eligible capital projects in future periods, issuance of long-term debt, and receipt of dividends from the City's government business enterprises (Toronto Hydro Corporation and Toronto Parking Authority).

Liabilities increased due to the build-up of development charges in the deferred revenues balance, issuance of long-term debt to finance the acquisition of tangible capital assets, an increase in the City's employee benefits liability in recognition of services rendered by employees in the current year, and higher remediation costs caused by inflation for the City's environmental and contaminated sites liabilities.

Net debt decreased on an overall basis due to the City recognizing more financial assets than liabilities in the current year. Although this downward trend is favourable for the City, it is important to note that the presence of this balance indicates that the City will have to raise additional revenues in the future to pay for its current obligations.

Non-financial assets increased during the year primarily due to the City's continued investments in its tangible capital assets for purposes of supporting service delivery to residents and businesses.

Revenue increased mainly due to increases in taxation rates, government grants which supported the City's response to the pandemic, municipal land transfer taxes collected as a result of high real estate sale volumes in the city, and development charges applied to eligible capital projects for community investment purposes. It is important to note that the City relied on government grants more significantly than in prior periods – in 2021, the City's government grants supported 35% of its operating expenses whereas in pre-pandemic years, government grants, on average, only supported 26% of its operating costs.

Expenses increased primarily as a result of the City's efforts in responding to the pandemic – more emphasis was placed on the delivery of essential and frontline services, including the operation of mass immunization clinics, expansion of the City's emergency shelter services to address public health guidelines, with additional costs also incurred to redeploy City personnel and support vulnerable sectors of the community. In addition, the City's focus on economic recovery led to greater emphasis being placed on the completion of various capital projects that required use of contracted services previously authorized by City Council, resulting in the recognition of increased amortization expenses for the tangible capital assets acquired in 2021.

Annual surplus represents an accrual accounting based balance, comprised of the excess of revenues over expenses recognized on an accrual accounting basis. In 2021, the City's COVID-19 operational pressures were offset through government grants from senior levels of governments, in order to respond to ongoing financial pressures caused by the pandemic and sustain the City's provision of critical frontline services.

When reviewing the City's annual surplus, it is also important to note that this represents an accounting surplus. The City, as noted in earlier sections, prepares its Consolidated Statements using an accrual basis of accounting in order to comply with PSAS' financial reporting requirements. However, the City's budget is prepared using the modified cash basis of accounting. When comparing the annual surplus reflected in the City's Consolidated Statements to the variance reported in the City's budget documents, it is essential to recognize that the City applies different principles to prepare the two separate documents. The Consolidated Statements consider the long-term financial impacts associated with the City's activities, decisions and transactions. Examples of these impacts include the City's recognition of tangible capital assets and their associated amortization expenses, as well as recognition of long-term obligations, such as financial commitments tied to the City's contaminated sites and employee benefit obligations.

Overview of the City of Toronto Audited SF Statements

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 debt 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.

Currently, the City has four (4) active and separate sinking fund portfolios supporting thirty nine (39) individual debenture issues at varying stages of maturity. The City's 5.0% sinking fund was closed due to the related debt maturing in 2021.

Highlights of the SF Statements

Sinking fund assets as at December 31, 2021 amounted to \$2.0 billion. The assets consist of cash 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. These assets represent amounts held to discharge City debt of \$8.4 billion (2020: \$8.1 billion) maturing between 2023 and 2051.

Sinking fund liabilities of \$1.8 billion consist mainly of the actuarial requirements of the sinking fund to reach the required debt repayment value at maturity.

The net assets value of \$0.2 billion reflects the sinking funds' unrestricted 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. The unrestricted surplus is available to address shortfalls in earnings in future years or can be redirected by the Chief Financial Officer and Treasurer.

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 cash balances. In 2021, a \$417 million contribution was made to the sinking funds, which was recognized as revenue during the year. This contribution has been allocated to support the maturity of the City's debt, which has helped to reduce the City's overall liabilities. Revenues for 2021 decreased by \$99 million to \$443 million (2020: \$542 million) due to a decrease in investment income of \$103 million, which was offset by an increase in contributions of \$4 million.

The 2021 decrease in investment income of \$103 million is mainly attributable to these factors: a decrease of \$82 million in unrealized gain resulting from changes in overall market value and an average rate of return which was 1.30% lower in 2021 than in 2020.

When the balance required to meet the debt liability maturity requirements increases, the amount is expensed in the Statement of Operations. The \$481 million (2020: \$424 million) expensed in 2021 represents the annual increase in the liability amount.

Overview of the Consolidated TF Statements

A trust fund is a fund which consists of assets that have been conveyed or assigned to a trustee to be administered as directed by agreement or statute. As a result, a trustee holds title to the assets for the purpose of providing benefits and being accountable to a beneficiary. The City is the trustee of a number of trust funds that are to be used for specific purposes by the City or its Agencies and Corporations.

The City administers most of the trust funds included in these TF Statements, except for the Toronto Police Services Board and Toronto Police Services Board Mounted Unit Trust Funds, which are administered by the Toronto Police Services Board. Appendix D provides the description and purpose of each trust fund consolidated in the TF Statements.

As part of its fiduciary responsibilities, the Trust Administrator ensures that funds received are to be used only for the purpose specified by each trust agreement.

Highlights of the TF Statements

Trust fund assets are comprised of cash, investments, and amounts due from the City or Administrators, where applicable. Total assets as at December 31, 2021 amounted to \$116 million (2020: \$106 million) of which \$97 million (2020: \$86 million) was in the form of investments.

Trust fund balances as at December 31, 2021 amounted to \$116 million (2020: \$106 million). The difference between the trust fund assets and year-end fund balances represent liabilities, including accounts payable of \$170 thousand, of the trust funds.

Revenues, consisting of investment earnings and contributions, decreased by \$14 million in 2021 to \$27 million (2020: \$41 million). The investment income component of revenues stayed relatively consistent, but was lower than in previous years due to continued impacts of the pandemic on the market. Interest Income increased by \$0.3 million, while the contributions decreased by \$13 million.

Trust fund expenditures, which represent withdrawals from each individual fund, increased by \$9 million in 2021, as a result of increased withdrawals to support purchases of investments held in trust for the Toronto Atmospheric Fund.

The Consolidated Statement of Continuity of Fund Balances details the contributions, investment earnings, expenses and balances of each individual trust fund that form the consolidated fund balance of \$116 million on the Statement of Financial Position.

KPMG's 2021 Year-End Report to the Audit Committee

The City's Consolidated Statements, SF Statements, and TF Statements have been audited by KPMG LLP, who is responsible for applying sufficient and adequate audit testing in order to provide an independent opinion on the fair presentation of the financial statements and that the financial 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 by all stakeholders. KPMG has issued an unqualified audit opinion on the City's 2021 financial statements.

KPMG's Year-End 2021 Audit Findings Report will be presented separately to the Audit Committee.

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SIGNATURE

Heather Taylor
Chief Financial Officer and Treasurer



Andrew Flynn
Controller

ATTACHMENTS

- Appendix A: 2021 Audited Consolidated Financial Statements
- Appendix B: 2021 Sinking Funds Financial Statements
- Appendix C: 2021 Consolidated Trust Funds Financial Statements
- Appendix D: Trust Fund Account Descriptions as at December 31, 2021