

**TORONTO PORT AUTHORITY  
(Doing Business as PortsToronto)**

**MANAGEMENT'S DISCUSSION & ANALYSIS – 2014**

**(in thousands of dollars)**

**May 8, 2015**

*Management's discussion and analysis (MD&A) is intended to assist in the understanding and assessment of the trends and significant changes in the results of operations and financial condition of the Toronto Port Authority for the years ended December 31, 2014 and 2013 and should be read in conjunction with the audited financial statements and accompanying notes.*

**Summary**

The Toronto Port Authority, operating as PortsToronto (“Port Authority” or “TPA”) continued to be profitable in 2014. Net Income for the year was \$14,887, up 8.9% from \$13,665 in 2013.

In 2014, all four of the main business areas of the Toronto Port Authority were profitable on an operating basis. This is shown on page 35, Note 19, of the 2014 Audited Financial Statements.

This is the fourth year that the Port Authority has presented its financial statements under International Financial Reporting Standards (“IFRS”). The accounting policies set out in Note 2 of the 2014 Audited Financial Statements have been applied in preparing the financial statements for the year ended December 31, 2014, and in the comparative information presented in these financial statements for the year ended December 31, 2013.

**Introduction**

The TPA was incorporated on June 8, 1999 as a government business enterprise under the *Canada Marine Act* as the successor to The Toronto Harbour Commissioners.

The Toronto Port Authority is responsible for operating the lands and harbour it administers in the service of local, regional and national social and economic objectives, and for providing infrastructure and services to marine and air transport to help realize these objectives.

The TPA is an important part of the Southern Ontario Gateway as it is one of five ports of significance in the province, while the Billy Bishop Toronto City Airport (“BBTCA” or “Airport”) is one of four airport facilities (Pearson, Waterloo, Hamilton) in the region with the capability to provide international service. In this regard, the TPA is and will remain an important factor in the economic health of Southern Ontario.

*(in thousands of dollars)*

The main operations of the Port Authority are Port Operations, the Outer Harbour Marina (“OHM”), the BBTCA and Property/Rental.

The TPA owns and operates Marine Terminal 51 and Warehouse 52 (“Marine Terminals”) located at the foot of Cherry Street. The TPA also owns the International Marine Passenger Terminal (“IMPT”), which currently services the cruise ship industry and has been used as a location for film productions.

The TPA continues to promote a mixed usage of its Marine Terminals, including bulk handling and storage, general and project cargo, as well as container packing and unpacking services. With a solid economy and a growing population in Toronto and surrounding areas, there is renewed interest in the Port of Toronto. There are several projects related to mixed usage that the Port Authority is pursuing in 2015.

The financial performance of the Outer Harbour Marina remains positive and consistent. Demand for winter storage remained strong in the 2014-2015 winter season and summer berthing renewals also remain strong. Low interest rates continue to create an inducement encouraging consumers, led by people aged 45 to 65, to buy more and bigger recreational boats. New technology in both the power and sail categories is making it much easier for novice boaters to buy bigger boats. This is important as the Port Authority replaced its smaller twenty year old docks with an inventory of larger boat slips and is considering expanding the Marina to add 435 new and larger slips.

The Billy Bishop Toronto City Airport (BBTCA) has a competitive advantage in a market that includes Pearson International Airport (“Pearson”), Hamilton, Waterloo and Oshawa airports. BBTCA’s close proximity to downtown Toronto provides time sensitive, environmentally conscious travelers the predictable convenience and service they demand.

According to an Economic Impact Study released in February 2015 conducted by Intervistas Consulting Inc., a leading management consulting company, BBTCA generates \$2.1 billion in annual economic output and 6,220 jobs, which includes 1,860 directly associated with the Airport. The study also found that the ongoing operations of the Airport continue to “make a considerable contribution to local employment and the provincial economy.” The study was an update to the Economic Impact Study released in November 2012.

*(in thousands of dollars)*

Pedestrian Tunnel to Airport (Please see Note 16 (a) in the 2014 Audited Financial Statements)

On March 8, 2012, the Port Authority entered a Project Agreement with Forum Infrastructure Partners (“Forum”) to design, build, finance, operate and maintain a pedestrian tunnel (the “Pedestrian Tunnel”) under the Western Channel linking the mainland and the Airport. The Project takes the form of a twenty year Concession Agreement wherein the Port Authority will make Monthly Service Payments (“MSPs”) to Forum using a portion of the \$20.00 Airport Improvement Fee (“AIF”) collected from enplaning (departing) passengers at the Airport. For comparison purposes, each passenger at Pearson currently pays an AIF of \$25.00 per departure. In addition, Pearson charges a connecting passenger fee of \$4 per passenger, while BBTCA currently does not have such a charge.

The construction cost of the Pedestrian Tunnel is contracted at \$82.5 million and it is expected to be substantially complete in spring 2015. Ownership in the Pedestrian Tunnel is vested in the Port Authority.

The cumulative capital asset value recorded to the end of December 31, 2014 on the Pedestrian Tunnel was \$111,356 (2013- \$76,166) and is included under Capital Assets as work-in-progress. This includes the construction cost as well as other costs such as engineering, legal, consulting and financing during construction.

30 Bay /60 Harbour Street Development Project (Please see Note 17 in the 2014 Audited Financial Statements)

On September 9, 2013 the Toronto Port Authority signed an Agreement with Oxford Properties to develop the approximately 1.8 acre site at 30 Bay Street and 60 Harbour Street, owned by the Port Authority. The development will consist of an office building and retail podium on the site and include the refurbishment of the historic Toronto Harbour Commission building. The Port Authority’s contribution to the project is the property. Oxford will be performing the planning and development phases as part of the Agreement. Certain conditions have to be met before the project can proceed.

Proposed Runway Extension Project (Please see Note 18 in the 2014 Audited Financial Statements)

In April 2013, Porter Airlines initiated a process to seek approval to fly CS-100 aircraft at Billy Bishop Toronto City Airport which would involve a lifting of the jet-ban and a 200-metre extension of the land mass on either end of the main Runway 08-26.

The extension of the runway would require amendments to the Tripartite Agreement. The City of Toronto began an assessment in April 2013 to review and ultimately render a decision on Porter Airline’s Proposal (“Proposal”). At that time, the Port Authority determined it would not make its own determination on the Proposal until City Council had made its decision. If City Council were to approve the introduction of jets at the airport, the Port Authority would then undertake its own review of the Proposal to confirm that the

*(in thousands of dollars)*

associated construction and operations would meet a strict, ten-point “Do No Harm” criterion.

On April 1, 2014, Toronto City Council decided to defer their vote regarding the introduction of jet aircraft at Billy Bishop Airport to 2015, pending the completion of certain work and studies that would inform future discussion on the Proposal. These studies included the PortsToronto completion of an Environmental Assessment (EA), Runway Design and a Master Planning Exercise, which contemplates the introduction of jets at the Airport.

Costs incurred for these studies are recorded in work-in-progress as a capital asset. In the event that the Porter Proposal does not proceed, the results and information from the Environmental Assessment, Runway Design and Master Plan will be utilized for future projects such as Runway End Safety Areas (RESA), which may be mandated by Transport Canada in the near future for certain qualifying runways at Canadian airports.

#### Payments to the Government Stakeholders

The TPA annually pays a charge on Gross Revenue to the federal government based on the calculated gross revenue in each fiscal year. For 2014, the amount paid to the federal government was \$2,425 (2013 - \$2,411). In addition, the TPA pays Payments-in-lieu of Taxes (“PILTs”) to the City of Toronto. The PILTs amount accrued by TPA for 2014 was \$2,932 (\$2,866 in 2013). The amounts paid and accrued to the federal government and to the City of Toronto together total \$5,357 in 2014 and \$5,277 in 2013, representing 10.6% and 10.5% of the Port Authority’s Operating Revenue, respectively in fiscal year 2014 and 2013.

*(in thousands of dollars)*

**Fiscal Period – January 1 to December 31, 2014 versus 2013**

**Consolidated Statement of Operations and Comprehensive Income (Financial Statements – Page 3)**

Revenues totaled \$50,515 in 2014, an increase of \$222 over 2013 Revenue of \$50,293. Expenses decreased by \$1,432 in 2014 versus 2013, from \$34,077 to \$32,645.

Revenues reported as Port Operations, Outer Harbour Marina, Airport, Property and Other, not including the Airport Improvement Fees, were \$31,769 in 2014 versus \$32,293 in 2013, a decrease of \$524. The main reason for the decrease was Airport revenue, with a year over year decline of \$713. Port Operations was higher by \$229, the Marina by \$8 and Property by \$21. Investment Income was lower by \$69.

In Expenses, Wages, Salaries and Employee Benefits were \$10,461 in 2014, lower by \$783 versus 2013. The Airport was \$458 lower, due primarily to lower Pension expenses. The Outer Harbour Marina and Property and Other were also lower due to lower Pension Expenses, while Port Operations was lower due to less terminal activity. Corporate was higher by \$131 due to increases in the Communications and Human Resources departments.

Repairs and Maintenance for the Port Authority increased in 2014 by \$216, from \$3,982 in 2013 to \$4,198 in 2014. This was primarily due to required maintenance on Airport Field Equipment.

Professional and Consulting Fees decreased by \$312 in 2014 to \$2,052, due to lower legal fees at the Airport, partially offset by higher legal fees in Port Operations.

Amortization increased in 2014 over 2013 by \$247, as additional assets are being brought into use and amortized at all business areas of the Port Authority.

Other Operating and Administrative Expenses were down by \$801 in 2014 versus 2013, to \$10,613. The decrease resulted from lower Airport operating expenses, with higher expenses incurred in 2013 related to the resolution of the City of Toronto Payments in Lieu of Taxes to the City of Toronto issue for the Airport.

**Please refer to page 35, Note 19 as a reference for the following discussion.**

In 2014, all four of the main business areas of the Toronto Port Authority were profitable on an operating basis.

Included in Net Income from Operations are the Airport Improvement Fees collected from enplaning/departing passengers. The number of enplaned and deplaned passengers in 2014 combined (not including connecting passengers) increased over 2013, but on a flatter curve than in prior years. Enplaned and deplaned passengers in 2014 totaled 1,996,494<sup>1</sup> versus 1,911,632<sup>1</sup> in 2013. With connecting passengers included, the numbers for enplaned and deplaned passengers were 2,428,282<sup>1</sup> and 2,294,422<sup>1</sup> in 2014 and 2013, respectively. It should be noted that the Airport Improvement Fees are restricted revenues that can only be used for Airport capital projects and expenditures.

*(in thousands of dollars)*

The operating bottom line for Port Operations was Net Income of \$1,155 in 2014. This was higher than 2013 by \$86, as property revenues, cargo dues and shore power charges were higher in 2014. Total Port tonnage was 2,006,471<sup>1</sup> in 2014 versus 1,556,025<sup>1</sup> in 2013, an increase of 29.0%. This was primarily due to higher salt and aggregate cargo tonnages coming into Port.

The Outer Harbour Marina continued its steady performance, with an operating profit of \$1,183, a decrease of \$167 from the operating profit of \$1,350 in 2013.

Property and Other accounted for an operating profit of \$521 in 2014, an increase of \$128 versus 2013.

Investment Income was \$363 in 2014 versus \$432 in 2013. Corporate Services expenses were up \$725 and the Charge on Gross Revenue increased by \$14. The increase in Corporate Services expenses related to higher Public Affairs expenses and expenses incurred by the Port Authority to meet its obligations under the Canada Marine Act.

Payments in Lieu of Taxes to the City of Toronto increased in 2014 to \$2,932 and there was a Loss on the Interest Rate Swap of \$51. These items accounted for the remaining change in the overall bottom line. Net Income was \$14,887 in 2014 versus \$13,665 in 2013, an increase of \$1,222. Comprehensive Income decreased from \$25,185 in 2013 to \$10,496 in 2014. This resulted from a large change in the remeasurement of the net defined benefit pension liability, which is further explained on page 25, Note 8.

### Port Operations

Port revenues are generated from the operation of the Marine Terminals and include terminal handling charges, container services, terminal berthing and ships services. In addition, revenue is generated from the IMPT, including charges for cruise ships and filming. From waterside, there are Harbour User Fees paid by Tour and Charter boats and Cargo Dues paid by large industrial ships. Finally, the Works & Environmental Services department generates revenue from services provided to Port users and other general customers.

Port revenue was up in 2014 by \$229 versus 2013, as Property Revenue, Cargo Dues and Shore Power Charges increased, while Terminal Handling Fees were lower due to a reduction in TPA's activities at the Marine Terminal operation.

Port expenses increased in 2014 versus 2013 by \$143, primarily due to higher Wages, Salaries and Benefits and Legal Fees, offset by lower Operating and Administrative expenses.

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<sup>1</sup> *Actual number, not rounded to the nearest thousand.*

*(in thousands of dollars)*

### Outer Harbour Marina (“OHM”)

The occupancy rate for summer berthing at the OHM remained at around 95% in 2014 and stayed at 100% for winter storage. The annual turnover rate remained low in 2014 at approximately 5% for summer contracts.

In addition to berthing and storage, marina services include shore power, pump-outs, power wash, fresh water and the sale of fuel and other products. There is also a 50-ton travellift for haul out and launch, and masting/demasting services.

Revenues at the Outer Harbour Marina were up \$8, as winter storage fees increased in 2014 versus 2013. A trend towards larger boats as well as rate increases continues to push revenues higher.

Expenses were up \$175 from 2013 to 2014, as Financing Costs, Operating and Administrative expenses and Repairs and Maintenance expenses were higher.

### Billy Bishop Toronto City Airport (“Airport”)

In 2014, operations at the Airport continued to grow, although at a somewhat slower pace than the previous seven years when Porter Airlines were adding aircraft and destinations to their service offering and Air Canada – Sky Regional began their service. The two main revenue sources at the Airport are the Airport Operating Fees charged based on slot allocation and usage and Airport Improvement Fees, currently at \$20.00, collected from enplaning/departing passengers. The Airport Improvement Fee is funding the Airport’s ongoing capital expenditure program, including debt service on the existing Bank Loans.

The increase in passenger volumes and Airport activity continued to drive Airport revenues although 2014 revenue was only up marginally to \$39,567 versus \$39,534 in 2013, an improvement of just \$33. The number of Enplaned Passengers paying AIF in 2014 was 993,896, up from 954,463 in 2013, or 4.1%. This generated \$18,746 in AIF in 2014 versus \$18,000 in 2013.

On the expense side, there was a decrease of \$2,382 in 2014, due primarily to a decrease in expenses related to a resolution with the City of Toronto on Payments in Lieu of Taxes to the City of Toronto and Legal Fees related to labour matters that occurred in 2013.

### Property and Other

Revenues from ancillary property holdings and other sources, such as filming, were higher in 2014, by \$21. The small increase was due to an increase in property rent.

Expenses decreased \$107 in 2014 versus 2013, mainly due to a reduction in Wages, Salaries and Benefits from reduced staffing levels.

*(in thousands of dollars)*

### Investments

Investment Income was down \$69 in 2014 versus 2013, as investment rates on reserves were lower in 2014.

### Corporate Services

Corporate Services support the operations of the Toronto Port Authority by providing general administrative support and services. These include executive, finance, accounting, human resources, communications, information technology, legal, risk management, promotion and the functioning of the Board of Directors. General expenses, related to TPA, but not related to any particular operation are assigned to Corporate Services.

Expenses in Corporate Services increased in 2014 by \$725, compared to 2013. Wages, Salaries and Benefits, Public Affairs, Consulting and expenses related to the Canada Marine Act were higher in 2014. The TPA continued to support and make investments in the Toronto waterfront community.

### Payments-in-Lieu of Taxes (“PILTs”) to the City of Toronto (Please see Note 10 in the 2014 Audited Financial Statements)

An amount of \$2,932 has been accrued for 2014 for PILTs payments to the City of Toronto. This is in addition to the \$16,875 already paid to the City for years 1999 through 2014. Of the eighteen Port Authorities in Canada, the TPA pays one of the highest PILTs amounts as a percentage of gross revenue, ranking number two.

TPA and the City have settled PILTS to the City of Toronto for BBTCA. The parties are working together on a potential settlement of the values for the additional PILT eligible properties.

### Gain/(Loss) on Interest Rate Swap

The TPA had been following hedge accounting rules on a “critical terms match” basis under GAAP. Under IFRS, the Swap was reevaluated and did not meet IAS 39 requirements in terms of necessary documentation and testing/assessment in 2010 and 2011. The unamortized accumulated other comprehensive loss due to losses in derivatives previously designated as cash flow hedge as at December 1, 2009 was \$1,087. This loss is being amortized over the remaining term of the Swap until maturity on January 4, 2022. As of January 1, 2012, the ineffective portion of the gains and losses on the Swap were recognized in the Statement of Operations. The total impact of gains and losses on derivatives including amortization in 2014 was (Loss 2014 - \$51) (Gain 2013 - \$315). The hedge for the Swap was redesignated effective January 1, 2012 and now continues to be effective.

*(in thousands of dollars)*

**Consolidated Statement of Changes in Equity (Financial Statements – Page 4)**

The Statement of Changes in Equity had an opening balance in Equity on January 1, 2013 of \$70,323, which included an Accumulated Other Comprehensive loss of \$2,734. The ending balance as at December 31, 2013 included the Net Income for the year of \$13,665, plus the Unamortized Gain and Past Service Costs – IAS19R of \$11,533, Amortization of the Accumulated Loss on Derivative Interest of \$91, plus the Gain on Interest Rate Swap – Effective Portion of \$138, plus the Unrealized Loss on Available for Sale Assets of \$151, for a closing Equity balance as at December 31, 2013 of \$95,599. The Amortization of \$91 is included in the Loss on Interest Rate Swap in the Statement of Operations and Comprehensive Income.

The ending balance as at December 31, 2014 included the Net Income for the year of \$14,887, plus a Pension Loss as a result of Remeasurement of the liability - IAS19R of \$4,141, plus Amortization of the Accumulated Loss on Derivative Interest of \$91, plus the Loss on Interest Rate Swap – Effective Portion of \$189, plus the Unrealized Loss on Available for Sale Assets of \$61 for a closing Equity balance as at December 31, 2014 of \$106,186. The Amortization of \$91 is included in the Loss on Interest Rate Swap in the Statement of Operations and Comprehensive Income.

**Consolidated Statement of Financial Position (Financial Statements – Page 5)**

Cash and Cash Equivalents and Short-term Investments are separated into two groups, one being assets that are not restricted in use as to Business Unit, and the other, identified as AIF Restricted that can only be used for Capital Expenditures at Billy Bishop Toronto City Airport. Cash and Cash Equivalents and Short-term Investments have gone from \$16,548 at the end of 2013 to \$21,492 as at December 31, 2014, an increase of \$4,944. Cash and Cash Equivalents and Short-term Investments that are AIF Restricted have gone from \$13,867 at the end of 2013 to \$14,634 as at December 31, 2014, an increase of \$767. An analysis of the Statements of Cash Flows is included below.

Accounts Receivable increased from \$6,317 at the end of 2013 to \$6,838 at the end of 2014. The details of the increase are found on Page 17, Note 3 to the Audited Financial Statements. The increase in receivables of \$521 was due to a small increase in Trade Receivables, 2014 versus 2013.

Comparing December 31, 2014 to December 31, 2013, Inventories were higher by \$15 and Prepaid Expenses decreased by \$6.

The details on Capital Assets are found on Page 22 and 23, Note 7. Capital Assets increased by \$39,441 in 2014 and on a Net Book Value basis the increase was \$37,046, when amortization and outside funding for capital projects are taken into account.

*(in thousands of dollars)*

The details of the gross increase are as follows:

Pedestrian Tunnel Project	\$35,189
Port Operations	\$353
Outer Harbour Marina	\$142
Billy Bishop Toronto City Airport	\$3,468
Property & Other	<u>\$290</u>
Total	<u>\$39,441</u>

In addition to the Pedestrian Tunnel Project shown above, larger Capital Expenditures in 2014 included a Departure Level Escalator in the Airport Terminal and an Environmental Assessment related to the proposed runway extension project under Porter's Proposal.

Amortization allocated to the operations over the years is deducted from the Capital assets, as well as amounts received for capital funding from various sources

Accounts Payable and Accrued Liabilities have increased by \$2,055, from 2013 to 2014. This is mainly due to an increase in Trade Payables as a result of higher activities at the end of 2014 compared to 2013.

The Fair Value of the Interest Rate Swap represents the closing balance following the loss in value in 2014 of \$149.

The current portion of the Bank loan is the principal amount to be repaid in the next fiscal year, in this case 2015.

The liability for Payments in Lieu of Taxes to the City of Toronto is the amount recognized as payable to the City of Toronto. Page 29 and 30, Note 10 describes the status of the PILTs to the City of Toronto.

Unearned Revenue did not change, 2014 versus 2013. This liability records the amount of Unearned Marina revenue the Port Authority will provide to customers by way of services in the upcoming year, as well as Unearned Harbour Permits and Unearned Rents.

The Bank Loans are described on Page 28, Note 9 (a).

The Pedestrian Tunnel Concession Liability is described on Page 33, Note 16 (a). As at December 31, 2014, the Pedestrian Tunnel Project was 93% complete and an asset of \$93,065 has been included as part of Capital under work in progress. The related liability as of December 31, 2014 was \$64,713.

Employee Benefit Liabilities represents the liability recognized for Port Authority Benefit Plans and are described on Pages 23 to 27, Note 8.

*(in thousands of dollars)*

Equity represents the difference between Assets and Liabilities. Equity increased in 2014 by \$10,587, as detailed on the Statements of Changes in Equity on Page 4.

The financial liquidity of the Port Authority remains strong, with a Current Ratio (Current Assets divided by Current Liabilities) of 2.37 as at December 31, 2014. This is a slight improvement over the Current Ratio as at December 31, 2013 of 2.34.

The financial performance ratio also remained strong, with a Profit Margin (Net Income divided by Gross Revenue) of 29% as of 2014 compared to 27% in 2013.

### **Consolidated Statement of Cash Flows (Financial Statements - Page 6)**

The Statements of Cash Flows begins with the Net Income reported in the Statement of Operations and Comprehensive Income and adds back any non-cash items. These include Amortization, Employee Future Benefit Expense, the Unamortized Gain and Past Service Costs – IAS19R, Interest Expense offset by Bank Interest Paid, AIF Restricted Cash and the (Gain)/Loss on the Derivative Designated as a Cash Flow Hedge.

An amount is then added or deducted for non-cash working capital. In 2014, this amount resulted in an increase in cash of \$900. This was due to an increase in Accounts Payable and Accrued Liabilities of \$2,055 and a decrease in Prepaid Expenses of \$6, offset by an increase in Accounts Receivable of \$521, an increase in Inventories of \$15 and a decrease in Payments in Lieu of Taxes to the City of Toronto of \$625.

Investing Activities and Financing Activities are then listed. Investing Activities include a decrease in Long-term Investments, a decrease in Short-term Investments and the Acquisition of Capital Assets listed above. Financing Activities include items related to Pedestrian Tunnel Project and the Bank Loans.

The end result is the Cash and Cash Equivalents position increased in 2014 by a total of \$8,711 from \$27,415 to \$36,126. The balance as at December 31, 2014 is a combination of Cash and Cash Equivalents – TPA \$21,492 and Cash and Cash Equivalents – AIF Restricted \$14,634, an increase of \$7,944 and \$767, respectively. The TPA continues to invest its cash resources in infrastructure improvements that benefit all of its business operations.

### **Board of Directors Governance**

The TPA is governed by a nine member Board appointed as per subsection 14 (1) of the Canada Marine Act, and as per section 4.6 of the Letters Patent issued to the Toronto Port Authority. There are six appointments by the Governor-in-Council as nominated by the Minister of Transport in consultation with the user groups, one appointment by the Governor-in-Council as nominated by the Minister of Transport, one appointment by the Province of Ontario and one City of Toronto appointment to the Board of Directors. There are five (5) Committees of the Board of Directors, namely the Board Executive Committee, the Audit & Finance Committee, the Governance, Nominating & Human Resources Committee, the Communications & Outreach Committee and the Pension Committee. The Chairmanship of the Board of Directors remained unchanged throughout 2014, with Mr. Mark McQueen in the position since January 21, 2009.