

**NEWFOUNDLAND AND LABRADOR
GOVERNMENT SINKING FUND**

**Annual Report
For the Period
April 1, 2019 to March 31, 2020**

**NEWFOUNDLAND AND LABRADOR
GOVERNMENT SINKING FUND**

**PENSIONS AND DEBT MANAGEMENT DIVISION
DEPARTMENT OF FINANCE
CONFEDERATION BUILDING
P.O. BOX 8700
ST. JOHN'S, NL A1B 4J6**

Honourable Siobhan Coady
Deputy Premier
Minister of Finance
Government of Newfoundland and Labrador
Confederation Building
St. John's, NL
A1B 4J6

Dear Minister Coady:

As the Chair of the Board of Trustees responsible for the Newfoundland and Labrador Government Sinking Fund (NLGSF), I am pleased to submit the 2019-20 Annual Report. The Board is a category 3 government entity, and in accordance with the **Transparency and Accountability Act** is required to prepare an annual activity report to present information on its activities of the preceding year. As such, the Board of Trustees is accountable for the preparation of this report and for the results reported herein.

The mandate of the Board of Trustees for the NLGSF is to administer the sinking funds established by the Government of Newfoundland and Labrador for the repayment of the Provincial Government's debenture debt. During the 2019-20 fiscal year, the NLGSF earned net income of approximately \$86.5 million, which included a foreign exchange gain of \$14.8 million resulting from an increase in the value of the U.S. dollar. This represents a 5.79 per cent return on the Sinking Fund Equity.

Sincerely,



PAUL SMITH CPA, CA, CMA
Chair

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1.0 OVERVIEW

The Newfoundland and Labrador Government Sinking Fund (NLGSF) was created pursuant to the **Financial Administration Act** to consolidate sinking funds established for the repayment of the Provincial Government's debenture debt. The Provincial Government has established sinking funds for some of its long-term debenture issues and the annual contributions to these sinking funds are invested by the Board of Trustees, who are appointed by the Lieutenant Governor in Council to manage and control the day-to-day operation of the sinking funds. As of March 31, 2020, the Board of Trustees consisted of the incumbents in four senior public service positions within the Department of Finance:

Denise Hanrahan	Deputy Minister
Michelle Jewer	Comptroller General
Theresa Heffernan	Assistant Deputy Minister Financial Planning and Benefits Administration
Vacant	Director, Pensions and Debt Management
Thomas Nemec	Manager, Capital Markets and Financial Assistance

The NLGSF operates with a March 31 fiscal year end and the results of its activities are fully consolidated in the Provincial Government's annual financial statements.

1.1 Mandate

The mandate of the Board of Trustees is to manage and control the operational activities of the NLGSF and the sinking funds of certain crown corporations where the Provincial Government has guaranteed the related debt (i.e. Newfoundland and Labrador Municipal Financing Corporation and the Eastern Regional Integrated Health Authority). These activities include establishing investment policy, investment of funds and the monitoring of such. These funds are invested in accordance with the **Financial Administration Act**, primarily in bonds, debentures or other securities issued or guaranteed by the Government of Canada, Provincial Governments within Canada or a chartered bank. The goal is to earn the maximum return from investment of the portfolio while ensuring security of the funds.

1.2 Sources of Funding

For debenture issues, which have sinking fund requirements, the Provincial Government makes the required sinking fund contributions to the operating bank account managed by the Board of Trustees. In 2019-20, these sinking fund payments amounted to \$44,531,000. Sinking fund contributions are invested and the interest earnings, less an amount to cover administrative costs, are re-invested.

The NLGSF's day-to-day activities are managed by employees of the Department of Finance and the Sinking Fund is invoiced quarterly by the Provincial Government for reimbursement of these expenses on a cost-recovery basis.

1.3 Operational Information

The NLGSF earned net income of approximately \$86.5 million during 2019-20, after a foreign exchange gain of \$14.8 million that resulted from an increase in the value of the U.S. dollar. Any gains or losses resulting from foreign currency translations will not be realized until such time that the U.S. assets are converted to Canadian dollars. Special purpose financial statements for the year ending March 31, 2020, are included in this report.

The 2017-2020 Activity Plan, as well as previous annual reports, are available online at www.fin.gov.nl.ca.

2.0 REPORT ON PERFORMANCE

In accordance with the Board's mandate, the following objective was identified for the 2019-20 fiscal year, which focuses on the primary activities of establishing investment policy; and the investment and monitoring of funds.

Objective: By March 31, 2020, Board of Trustees will have continued with the prudent investment of the assets of the fund.

Indicators: The assets of the fund prudently invested in accordance with the **Financial Administration Act**, as evidenced by the completion of periodic reviews of reports to the Board.

Results: The Board completed its review of an annual report which, in addition to financial results of the Fund, highlighted the investing activity of the Fund. This review ensured that the assets of the Fund were prudently invested in accordance with the **Financial Administration Act** and with the Board's mandate.

3.0 OPPORTUNITIES AND CHALLENGES

The unpredictable nature of the investment market will continue to challenge the Board of Trustees to ensure that its investment strategy maximizes the rate of return earned on its investment portfolio, while at the same time protecting the security of the sinking funds. A slow global economic recovery with a low-interest-rate environment continues to restrict the earning potential of the investment portfolio.

4.0 FINANCIAL STATEMENTS – Please see attached.

**NEWFOUNDLAND AND LABRADOR
GOVERNMENT SINKING FUND**

FINANCIAL STATEMENTS

MARCH 31, 2020



OFFICE OF THE AUDITOR GENERAL
NEWFOUNDLAND AND LABRADOR

INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees of the
Newfoundland and Labrador Government Sinking Fund
St. John's, Newfoundland and Labrador

Opinion

I have audited the financial statements of the Newfoundland and Labrador Government Sinking Fund (the Fund), which comprise the balance sheet as at March 31, 2020, the statements of statutory contributions, retained earnings, revenues and expenses and cash flows, schedule of investments and notes to the financial statements, including a summary of significant accounting policies and other explanatory information.

In my opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Fund as at March 31, 2020 and the results of its operations and its cash flows for the year ended in accordance with the accounting policies described in Note 1 to the financial statements.

Basis for Opinion

I conducted my audit in accordance with Canadian generally accepted auditing standards. My responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of my report. I am independent of the Fund in accordance with the ethical requirements that are relevant to my audit of the financial statements in Canada, and I have fulfilled my other ethical responsibilities in accordance with these requirements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Emphasis of Matter - Basis of Accounting and Restriction on Use

Without modifying my opinion, I draw attention to Note 1 to the financial statements which describes the basis of accounting. These financial statements are prepared solely for the information of the Fund and the Government of Newfoundland and Labrador to meet their information needs under Section 39 of the Financial Administration Act and under the various debentures which require the establishment of sinking funds. As a result, the financial statements may not be suitable for another purpose. My report is intended solely for the use of the Fund and the Government of Newfoundland and Labrador and should not be used by anyone other than the specified users.

Independent Auditor's Report (cont.)

Other Information

Management is responsible for the other information. The other information comprises the information included in the annual report, but does not include the financial statements and my auditor's report thereon. The annual report is expected to be made available to me after the date of this auditor's report.

My opinion on the financial statements does not cover the other information and I will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, my responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the financial statements or my knowledge obtained in the audit, or otherwise appears to be materially misstated. When I read the annual report, if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with the accounting policies described in Note 1 to meet the information needs of the Fund and the Government of Newfoundland and Labrador under section 39 of the Financial Administration Act and under the various debentures which require the establishment of sinking funds, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Fund or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Fund's financial reporting process.

Independent Auditor's Report (cont.)

Auditor's Responsibilities for the Audit of the Financial Statements

My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Fund's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Fund to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

Independent Auditor's Report (cont.)

I communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

A handwritten signature in black ink, reading "Sandra Russell". The signature is written in a cursive, flowing style.

SANDRA RUSSELL, CPA, CA
Auditor General (A)

September 22, 2020
St. John's, Newfoundland and Labrador

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND**BALANCE SHEET**

As at March 31

2020

2019

(000's)

(000's)

ASSETS**Current**

Cash	\$ 223,080	\$ 95,826
Term deposits and short-term investments	4,983	106,904
Interest and other receivables		
Province of Newfoundland and Labrador - guaranteed	16,878	13,174
Other	276	6,716

245,217

222,620

Investments, at amortized cost (Schedule)

Cost	1,171,751	1,251,647
Accumulated amortization of discounts and premiums	78,808	76,157

1,250,559

1,327,804

\$ 1,495,776

\$ 1,550,424

LIABILITIES AND SINKING FUND EQUITY**Current**

Accounts payable and accrued liabilities	\$ 10	\$ 11
Due to Province of Newfoundland and Labrador	30	3

40

14

Sinking fund equity

Accumulated statutory contributions	798,515	821,240
Retained earnings	697,221	729,170

1,495,736

1,550,410

\$ 1,495,776

\$ 1,550,424

See accompanying notes

Signed on behalf of the Board:


Chairperson and Trustee
Trustee

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND
STATEMENT OF STATUTORY CONTRIBUTIONS
For the Year Ended March 31

	2020	2019
	(000's)	(000's)
Balance, beginning of year	\$ 821,240	\$ 768,398
Add: receipts for the year	44,531	44,119
<u>Foreign currency translation adjustment (Note 2)</u>	<u>15,738</u>	<u>8,723</u>
	881,509	821,240
<u>Statutory contributions applicable to matured/redeemed debentures</u>	<u>(82,994)</u>	<u>-</u>
Balance, end of year	\$ 798,515	\$ 821,240

See accompanying notes

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND**STATEMENT OF RETAINED EARNINGS****For the Year Ended March 31**

	2020	2019
	(000's)	(000's)
Balance, beginning of year	\$ 729,170	\$ 652,099
Net income for the year	86,542	73,888
<u>Foreign currency translation adjustment (Note 2)</u>	<u>11,320</u>	<u>3,183</u>
	827,032	729,170
<u>Retained earnings applicable to matured/redeemed debentures</u>	<u>(129,811)</u>	<u>-</u>
<u>Balance, end of year</u>	<u>\$ 697,221</u>	<u>\$ 729,170</u>

See accompanying notes

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND
STATEMENT OF REVENUES AND EXPENSES
For the Year Ended March 31

	2020	2019
	(000's)	(000's)
REVENUES		
Interest income		
Debentures	\$ 49,156	\$ 53,978
Term deposits and short-term investments	416	618
Other	3,526	3,761
Gain on sale of securities	13,268	-
	66,366	58,357
Amortization of foreign currency translation gains (Note 2)	14,783	10,438
Amortization of discounts and premiums	5,628	5,370
	86,777	74,165
EXPENSES		
Salaries and benefits	131	154
General	104	123
	235	277
Net income	\$ 86,542	\$ 73,888

See accompanying notes

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND**STATEMENT OF CASH FLOWS****For the Year Ended March 31**

	2020	2019
	(000's)	(000's)
Cash flows from operating activities		
Net income	\$ 86,542	\$ 73,888
Adjustment for non-cash items		
Amortization of discounts and premiums	(5,628)	(5,370)
Amortization of foreign currency translation gains (Note 2)	(14,783)	(10,438)
Gain on sale	(13,268)	-
	52,863	58,080
Change in non-cash working capital	2,762	(2,509)
	55,625	55,571
Cash flows from financing activities		
Statutory contributions	44,531	44,119
Cash flows used in investing activities		
Purchase of investments	(214,200)	(116,395)
Proceeds from redemption and sale of investments	338,776	40,519
Payments of excess to Province upon maturing debentures	(212,805)	-
	(88,229)	(75,876)
Net increase in cash	11,927	23,814
Effect of foreign currency translation adjustment (Note 2)	13,406	4,348
Cash and cash equivalents, beginning of year	202,730	174,568
Cash and cash equivalents, end of year	\$ 228,063	\$ 202,730
Cash and cash equivalents include:		
Cash	\$ 223,080	\$ 95,826
Term deposits and short-term investments	4,983	106,904
	\$ 228,063	\$ 202,730

See accompanying notes

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND

SCHEDULE OF INVESTMENTS

As at March 31

2020

2019

	Face Value or Par (000's)	Amortized Cost (000's)	Face Value or Par (000's)	Amortized Cost (000's)
Canadian				
Province of Newfoundland and Labrador				
- guaranteed				
Province of Newfoundland and Labrador	\$ 418,224	\$ 453,951	\$ 218,224	\$ 254,850
Newfoundland and Labrador Hydro	35,248	39,572	35,248	40,011
Health Care Corporation (Eastern Health)	17,500	24,049	17,500	24,374
Coupons and residuals	271,264	195,389	269,464	186,262
	742,236	712,961	540,436	505,497
Other coupons and residuals	221,793	154,594	334,617	223,395
Other securities	60,812	69,665	116,017	130,925
	1,024,841	937,220	991,070	859,817
U.S.				
Province of Newfoundland and Labrador				
- guaranteed	132,851	137,329	192,530	199,348
Other securities	144,261	151,863	228,530	240,963
Coupons	23,121	21,840	26,089	23,985
Residuals	2,307	2,307	3,815	3,691
	302,540	313,339	450,964	467,987
Total investments	\$ 1,327,381	\$ 1,250,559	\$1,442,034	\$1,327,804

See accompanying notes

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND
NOTES TO FINANCIAL STATEMENTS
March 31, 2020

Authority

The Province of Newfoundland and Labrador issues debentures, most of which have sinking fund requirements. For debentures which have sinking fund requirements, the Province makes the required sinking fund payments (statutory contributions) to the Board of Trustees of the Newfoundland and Labrador Government Sinking Fund (the Fund). This is an unincorporated body formed under the Financial Administration Act. All members of the Board are full-time employees of the Province and are appointed by the Lieutenant-Governor in Council.

The Fund is not subject to Provincial or Federal income taxes.

1. Basis of accounting

These special purpose financial statements have been prepared by the Fund in accordance with the summary of significant accounting policies set out below to meet the information needs of the Fund and the Government of Newfoundland and Labrador under Section 39 of the Financial Administration Act and under the various debentures which require the establishment of sinking funds.

Summary of significant accounting policies

These financial statements have been prepared on the accrual basis of accounting. Outlined below are the significant policies followed.

(a) Cash and cash equivalents

Cash and cash equivalents include balances with banks, and term deposits and short-term investments with original maturities of three months or less.

Term deposits and short-term investments are recorded at cost which approximates market value because of the short term nature of the securities.

(b) Investment transactions

- (i) Purchases:** Investments are initially recorded at cost.
- (ii) Amortization:** Discounts and premiums are amortized on a straight-line basis from the date of purchase until maturity.
- (iii) Sales:** Sales of investments are at a negotiated selling price. Sales are recorded at the proceeds less the investment's average amortized cost, with any resulting gain or loss also recorded.
- (iv) Redemptions:** On occasion, investments held in the Fund will be called for redemption by the issuer. In such instances, a gain is recorded equal to the redemption proceeds less the investment's average amortized cost.

1. Basis of accounting (cont.)

Summary of significant accounting policies (cont.)

- (c) Maturity of a Province of Newfoundland and Labrador debenture issue for which a sinking fund has been provided:

(i) General

A sinking fund is created pursuant to the provisions of a debenture issue in order to provide funds to be used for redemption at debenture maturity. Statutory sinking fund contributions are invested in interest bearing securities and other investments. Both the contributions and the interest are used to pay debenture holders when debentures mature.

A record is maintained of statutory contributions received on account of each issue and of income allocated to each issue (retained earnings). The accumulated amount of an issue's statutory contributions and allocated income is called its Sinking Fund Value.

At the maturity of a debenture issue, accumulated statutory contributions are reduced by the total amount of statutory contributions received over the life of the debenture issue. Retained earnings are reduced by the excess of the Sinking Fund Value over statutory contributions received related to the debenture issue.

(ii) Cash flow

At maturity, cash is paid into a redemption bank account in an amount equal to the lesser of the total face value of the issue or the Sinking Fund Value of the issue, less the face value of the particular debenture issue being redeemed held in the Fund's investments. If the Sinking Fund Value of the issue is less than the total face value, the difference is paid into the redemption bank account by the Province.

- (d) Province of Newfoundland and Labrador debentures held by the Fund are cancelled upon the related sinking fund becoming fully funded. This occurs when the value of a sinking fund for a debenture issue equates to the outstanding principal amount of that issue. The Fund will return to the Province, for cancellation, any debentures of that issue held by the Fund. The cancellation of sinking fund assets results in a corresponding reduction in sinking fund equity.

(e) Interest income

Interest income is recorded on an accrual basis.

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND
NOTES TO FINANCIAL STATEMENTS
March 31, 2020

1. Basis of accounting (cont.)

Summary of significant accounting policies (cont.)

(f) Foreign currency translation

Assets, liabilities, revenues and expenses denominated in U.S. currency are translated as follows:

- (i) assets and liabilities are translated at the rate of exchange in effect at the balance sheet date; and
- (ii) revenues and expenses are translated at the rate of exchange in effect on the dates on which such items are recognized in income during the year, or an average of such.

Gains and losses resulting from foreign currency translation are amortized on a straight-line basis over the remaining life of each issue's sinking fund.

2. Effect of foreign currency translation

At March 31, 2020, the Fund held \$1,250,559,000 (2019 - \$1,327,804,000) in investments. These investments include \$220,864,000 denominated in U.S. currency (2019 - \$467,987,000).

The Fund assets, liabilities, statutory contributions and retained earnings denominated in U.S. currency are translated at the rate of exchange in effect at the balance sheet date. The Fund's revenues and expenses are translated at the rate of exchange in effect on the dates on which such items are recognized in income during the year, or an average of such.

In 2020 and in the previous fiscal year, the translation of assets denominated in U.S. currency at year end resulted in a net foreign exchange gain due to a increase in the value of the U.S. dollar. Any gains or losses resulting from foreign currency translations will not become realized until such time the assets denominated in U.S. currency should ever actually be converted to Canadian dollars. It is not the intention of the Fund that its U.S. assets will be converted into Canadian dollars.

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND
NOTES TO FINANCIAL STATEMENTS
March 31, 2020

2. Effect of foreign currency translation (cont.)

	<u>2020</u> (000's)	<u>2019</u> (000's)
The effect of the translation is as follows:		
Statutory contributions have increased by	\$ 15,738	\$ 8,723
Retained earnings have increased by	11,320	3,183
Net income increased by	14,783	10,438
Total impact of foreign currency translation	\$ 41,841	\$ 22,344

The effect of this amount on the Fund assets is as follows:

Investments have increased by	\$ 28,435	\$ 17,996
Cash has increased by	13,406	4,348
	\$ 41,841	\$ 22,344

The increase of \$13,406,000 (2019 - increase of \$4,348,000) is reflected in the Statement of Cash Flows because of its impact on the Fund's cash flow position. However, the other transactions did not have an impact on the Fund's cash flow position and are, therefore, not reflected in the Statement of Cash Flows.

3. Financial instruments

The Fund's short-term financial instruments recognized on the balance sheet consist of cash, term deposits and short-term investments, interest and other receivables, accounts payable and accrued liabilities, and due to Province of Newfoundland and Labrador. The carrying values of these instruments approximate current fair value due to their nature and the short-term maturity associated with them.

The Fund holds long-term investments which have an amortized cost of \$1,250,559,000 (2019 -\$1,327,804,000). The face value of these investments is \$1,327,381,000 (2019 - \$1,442,034,000). The policy and intention of the Board is to hold these long-term investments to maturity. Therefore, their reported value is current fair value to the Fund and there is no significant market risk associated with these investments.