

**Management's Discussion and Analysis and Financial  
Statements of the**

**Greater Toronto Airports Authority**

December 31, 2008 and 2007

**GREATER TORONTO AIRPORTS AUTHORITY  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED DECEMBER 31, 2008  
DATED MARCH 11, 2009**

**Forward-Looking Information**

*This Management's Discussion and Analysis ("MD&A") contains certain forward-looking information. This forward-looking information is based on a variety of assumptions and is subject to risks and uncertainties. Please refer to the section titled "Caution Regarding Forward-Looking Information" contained at the end of this MD&A for a discussion of such risks and uncertainties and the material factors and assumptions related to the forward-looking information.*

This report discusses the financial and operating results for the Greater Toronto Airports Authority ("GTAA" or the "Corporation") for the year ended December 31, 2008 and should be read in conjunction with the Financial Statements of the GTAA for the years ended December 31, 2008 and 2007 and the Annual Information Form for the year ended December 31, 2008. These documents provide additional information on certain matters which may or may not be discussed in this report. Additional information relating to the GTAA, including the Annual Information Form and the Financial Statements referred to above, is available on SEDAR at [www.sedar.com](http://www.sedar.com). The GTAA's Financial Statements and MD&A are also available on its website at [www.gtaa.com](http://www.gtaa.com).

## **CORPORATE PROFILE**

The GTAA was incorporated in March 1993 as a corporation without share capital, and recognized as a Canadian Airport Authority by the federal government in November 1994. The GTAA is authorized to operate airports within the Greater Toronto Area ("GTA") on a commercial basis, to set fees for their use and to develop and improve the facilities. In accordance with this mandate, the GTAA currently manages and operates Toronto Pearson International Airport (the "Airport" or "Toronto Pearson").

The responsibilities of the GTAA for the operation, management and development of Toronto Pearson are set out in the ground lease with the federal

government which was executed in December 1996 (the “Ground Lease”). The Ground Lease has a term of 60 years, with one renewal term of 20 years. The GTAA’s priorities are to operate a safe, secure and efficient Airport and to ensure that the facilities provide the necessary services, amenities, and capacity for current and future air travel requirements for the GTA.

## **BUSINESS STRATEGY**

The GTAA is focused on providing quality aviation facilities at Toronto Pearson, recognizing that the region’s demand for air travel is expected to continue to grow. To meet this anticipated demand the GTAA undertook the Airport Development Program (“ADP”), substantially completed in January 2007, as well as the redevelopment of Terminal 3 and continues to plan for additional future development.

Throughout 2008 the GTAA continued to implement its five-year (2007-2011) strategic plan. Based on the vision for the GTAA – “to be a leading airport company championing sustainable global access for the Greater Toronto Area” – the strategic plan focuses on three key strategic themes:

- Making Toronto Pearson more globally competitive;
- Enhancing the Airport’s role as a gateway; and
- Ensuring the long-term sustainability of the Corporation.

Guided by the strategic plan, initiatives undertaken in 2008 included process reviews to reduce operating expenses and generate efficiencies for the GTAA and its partners and customers, continued development of non-aeronautical revenues and staff development and training.

The GTAA is a non-share capital corporation and therefore has established a program to access the debt capital markets on an ongoing basis to fund its various capital programs. The criteria, covenants and restrictions for financing by the GTAA are set out in the master trust indenture (the “Trust Indenture”) and are described in the section on Liquidity and Capital Resources. The Airport now has sufficient capacity to meet projected air travel demands for several years and accordingly it is anticipated that over the next several years any additional indebtedness will be used to fund expenditures related to the repair and maintenance of existing facilities and smaller scale new capital investments to improve operations at the Airport or to generate additional non-aeronautical revenue, as described in the section on Capital Projects. In December 2007 the

GTAA published an Airport Master Plan outlining the expected growth in air travel demand over the 2008 to 2030 period and the development activities required at the Airport and in the region to meet that demand. Significant new capital expenditures and financing activities will be required by the GTAA over the term of the plan to meet the air travel needs of the region. However, in the near term there are no significant capital expenditures planned as current capacity is sufficient to meet demand.

## **SIGNIFICANT EVENTS**

A number of significant events transpired in 2008 which had an impact on the GTAA's operations or its financial results or which may affect future results. In addition to the events discussed in this section, certain construction projects were completed which are discussed in the section on Capital Projects, and certain events transpired with respect to the restructuring of Asset Backed Commercial Paper ("ABCP") held by the GTAA which are discussed in the section on Asset Backed Commercial Paper.

On February 11, 2008, the GTAA executed an amendment to the Ground Lease. The amendment changes the way that ground rent is calculated, replacing the previous calculation that was largely based on passenger traffic with one based on revenue. The new formula will be phased in so that in 2008 and 2009 ground rent will be \$141.5 million and \$138.7 million, respectively. Beginning in 2010 ground rent will be calculated as a percentage of annual revenue using the following formula:

- 0% of the first \$5.0 million of revenue;
- 1% of the next \$5.0 million of revenue;
- 5% of the next \$15.0 million of revenue;
- 8% of the next \$75.0 million of revenue;
- 10% of the next \$150.0 million of revenue; and
- 12% of any revenue in excess of \$250.0 million.

The GTAA will continue to be required to pay ground rent deferred in the 2003 to 2005 period. The payment is approximately \$4.2 million per year and continues until the end of 2015.

On February 13, 2008, the GTAA filed a shelf prospectus qualifying the issuance of up to \$2.0 billion of debt over a 25-month term for the purpose of funding

capital expenditures and reserve funds, repaying existing debt or for other approved uses.

On February 28 and 29, 2008 the employees of the GTAA represented by Public Service Alliance of Canada Locals 00004 and 00005 and the Canadian Auto Workers Local 2002 voted on the consolidation of the three bargaining units into one bargaining unit. On March 3, 2008 the results of the vote were announced and the Canadian Auto Workers (the "CAW") was given the mandate to represent the unionized employees of the Corporation with the exception of those employees represented by the Pearson Airport Professional Firefighters Association. During 2008 the GTAA and the CAW met to negotiate the consolidation of the three collective agreements affected by the bargaining unit consolidation. The parties were unable to agree on the terms of a consolidated collective agreement and the matter has been referred to the Canadian Industrial Relations Board (the "CIRB"). The CIRB hearing on this matter is scheduled to take place in May, 2009.

On April 17, 2008, the GTAA issued \$500 million of Series 2008-1 Medium Term Notes ("MTNs") with a term of ten years and a coupon of 5.26%. The proceeds of the issue were used to repay existing debt, to fund required reserve funds and to fund ongoing capital projects.

On June 2, 2008 the \$375 million Series 2003-1 MTNs matured and were repaid with a combination of funds raised through the Series 2008-1 MTN issue and reserve funds.

On June 19, 2008 the GTAA announced that beginning January 1, 2009 the landing fee charged to all-cargo flights would be 25% less than the landing fee charged to passenger flights.

On August 28, 2008, Zoom Airlines ceased operations and filed for bankruptcy protection. At the time of the bankruptcy, the GTAA was owed approximately \$2.0 million in aeronautical charges and Airport Improvement Fees ("AIF"). As a result of the GTAA obtaining a court order to seize and detain two of Zoom's aircraft, the full amount owing to the GTAA was paid by Zoom's aircraft lessors.

On October 10, 2008, the GTAA announced its aeronautical rates and charges for 2009. Effective January 1, 2009, landing fees were reduced by \$0.15 per tonne of the aircraft's maximum takeoff weight ("MTOW") to \$33.87 per tonne and general terminal charges were reduced by \$0.05 per seat to \$7.47 and \$9.34 per

seat for domestic and international flights respectively. In addition, the 2009 landing fee for all-cargo flights was reduced to \$25.47 per tonne from the 2008 rate of \$32.02 per tonne.

On October 24, 2008, the \$350 million Series 2006-2 MTNs matured and were repaid using a combination of cash and investments and a draw on the GTAA's syndicated bank credit facility.

On December 8, 2008 the GTAA issued \$325 million of Series 2008-2 MTNs with a term of five years and a coupon of 5.89%. The proceeds of the issue were used to repay existing debt, to fund required reserve funds and to fund ongoing capital projects.

Subsequent to December 31, 2008, on February 4, 2009 the GTAA repaid the \$250 million Series 2004-2 MTNs using a combination of cash and reserve funds.

On February 13, 2009 the GTAA announced that, effective June 1, 2009, the AIF for originating passengers would be increased by five dollars to \$25.00. The connecting passenger AIF remains unchanged at \$8.00.

## **OPERATING ACTIVITY**

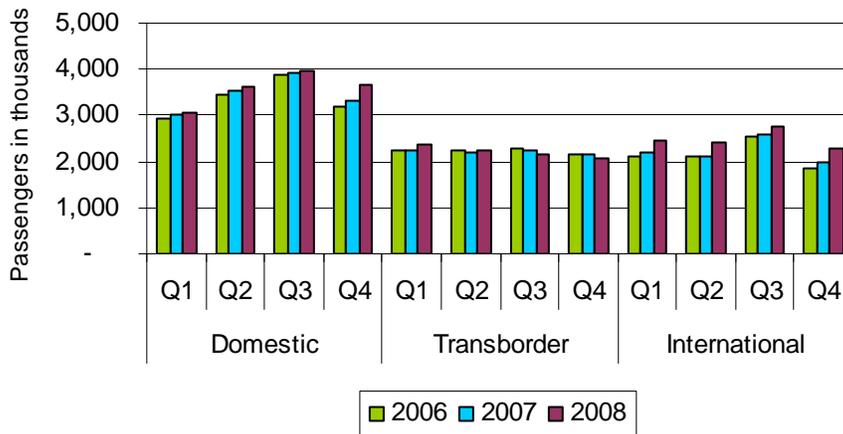
The GTAA monitors passenger activity levels and aircraft movements, including the type and size of aircraft, as both passenger and aircraft activity have a direct impact on financial results.

Total passenger traffic at the Airport in 2008 was 32.3 million passengers, an increase of 2.8% from the 2007 level of 31.4 million passengers. Passenger traffic at the Airport is generally categorized as belonging to one of three sectors: domestic, or passengers travelling within Canada; transborder, or passengers travelling between Canada and the United States; and international, or passengers travelling between Canada and destinations outside of Canada and the United States. Domestic passenger traffic in 2008 was 13.9 million passengers, a 1.1% increase over 2007. Transborder traffic was 8.8 million passengers, a 0.7% decrease from 2007, and international passengers numbered 9.6 million, a 9.1% increase over 2007.

Total passengers in each sector for 2008 and 2007 respectively were:

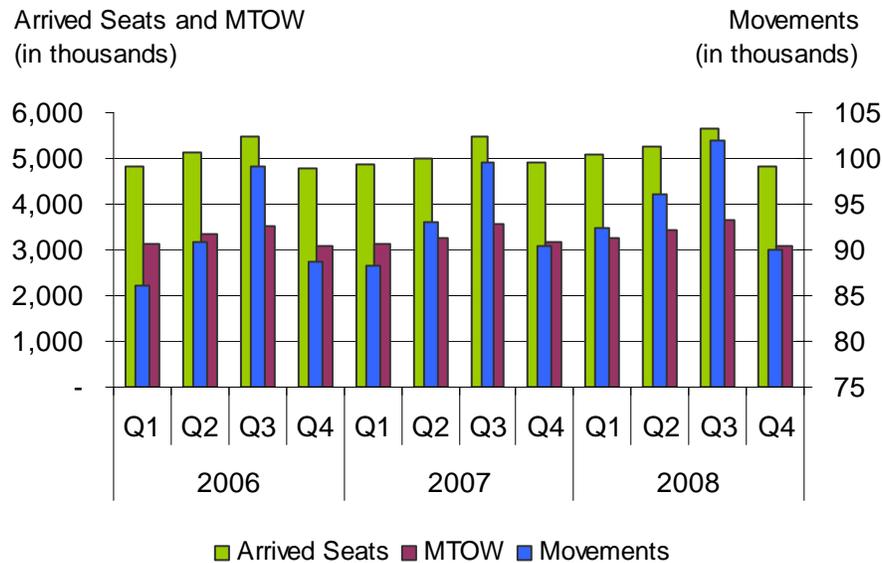
Passengers in millions	2008	2007
Domestic	13.9	13.7
Transborder	8.8	8.9
International	9.6	8.8
Total	32.3	31.4

While passenger activity fluctuates from year to year there is also some seasonal fluctuation in travel patterns including increased activity during the summer months and holiday periods. The following graph illustrates the quarterly passenger levels (in thousands), by sector, for the past three years:



Flight activity is measured by aircraft movements. The type and size of aircraft using the Airport determines the MTOW and the number of seats. These measures are used to calculate airline charges for each flight. Total movements in 2008 increased by 1.2%, from 425,500 in 2007 to 430,588. MTOW for 2008 was 13.4 million tonnes, as compared to 13.2 million tonnes in 2007, an increase of 2.1%. Total arrived seats increased 2.7% from 20.3 million in 2007 to 20.8 million in 2008. During the past several years airlines have been adjusting their fleet mixes and flight schedules in order to improve their financial performance, resulting in airline load factors, or the ratio of passengers to seats, steadily increasing. Reduced air travel demand in the latter part of 2008 and as projected for 2009 as a result of the slowing economy has caused many airlines to reduce capacity through reduced schedules and changes in aircraft type utilised on certain routes. This is expected to keep airline load factors high despite the anticipated slowing in demand which will have a negative effect on MTOW and arrived seats. It is expected that air carriers will continue to engage in these

capacity management techniques for the foreseeable future. The following graph illustrates the arrived seats, MTOW and movements (in thousands) for the past three years, by quarter:



In November 2006, the Government of Canada announced its “Blue Sky” policy whereby the federal government intends to proactively pursue opportunities to negotiate more liberalized agreements for international scheduled air transportation. Since that time a number of agreements have been put into place, including an agreement with the European Union. This policy initiative is expected to provide increased opportunities for passenger and cargo service to be added at Toronto Pearson as market demand warrants, although some legacy agreements continue to restrict open access to Toronto Pearson.

## RESULTS OF OPERATIONS

The following section discusses the GTAA’s approach in setting its aeronautical rates and charges, together with its financial results. In reviewing the financial results, it is important to note that the GTAA is a non-share capital corporation. Accordingly, the GTAA’s financial model is based on the premise that all funds, whether generated through revenue or debt, will be used for Airport operations, ancillary aviation-related activities, construction, repairs and maintenance, debt payments, reserve funds, and other activities within the GTAA’s mandate.

## **Rate Setting Approach**

The objective of the GTAA's rate setting approach is to break even on a modified cash basis after including the reserve and debt requirements as set out in the Trust Indenture. Aeronautical rates and charges are set by the GTAA annually to cover the projected operating costs on a break-even cash basis for each year. To calculate the rates and charges for a given year, projections are developed for measures of Airport operating activity such as passengers, MTOW and arrived seats, non-aeronautical revenue and operating costs. Operating costs include debt service for those assets that are operational, but do not include non-cash items such as amortization of capital assets. Capital costs, including interest for projects under construction, are funded through debt and are not included in the calculation of the aeronautical rates and charges. However, a notional amortization of debt, based on a 30-year amortization period, which is not included in the operating results, is included in the rate setting calculation.

The two components of the aeronautical rates and charges are the landing fee and the general terminal charge. Landing fees are set as a rate per tonne of MTOW to cover the projected operating costs associated with the airfield and groundside areas of the Airport, plus ground rent, payments-in-lieu of property taxes ("PILT") and specific debt service costs, offset by the projected non-aeronautical revenue and a specified amount of AIF revenue. Beginning January 1, 2009, all-cargo flights are charged a landing fee equal to 75% of the fee charged to passenger flights, reflecting the reduced use of facilities and resources by these flights. General terminal charges are set to cover the operating costs for the common areas in the passenger terminals as a rate per landed seat, regardless of whether the seat is occupied by a passenger. There is a premium on the general terminal charge for non-domestic flights to cover the additional costs, such as security and providing space and services to government inspection agencies, incurred by the GTAA in handling these flights. The common areas include holdrooms, check-in counters, passenger processing areas and arrival halls, but exclude space that is exclusively leased to airlines or other tenants.

## Net Operating Results

The GTAA's net operating results for the three years ended December 31, 2008, 2007 and 2006, are summarized in the following table:

(in thousands)	2008	2007	2006
Revenues	\$1,172,555	\$ 1,162,858	\$ 1,062,303
Operating expenses	555,238	552,026	560,120
Revenues over expenses <sup>1</sup>	617,317	610,832	502,183
Interest and financing costs, net	452,501	427,652	355,027
Amortization	210,730	227,130	225,934
Revenues under expenses	\$(45,914)	\$ (43,950)	\$(78,778)

Note 1: Revenues over expenses before interest and financing costs and amortization of capital assets

Revenues over expenses before interest and financing costs and amortization increased from \$610.8 million for the year ended December 31, 2007 to \$617.3 million for the year ended December 31, 2008. This increase reflects a \$9.7 million increase in revenues driven by increased non-aeronautical revenues, offset by a decrease in aeronautical revenues due to reduced aeronautical rates introduced in 2008. The revenue increase was offset by an increase in goods and services expense when compared to 2007. Interest and financing costs were \$452.5 million for 2008 as compared to \$427.6 million for 2007, reflecting reduced interest expense, offset by lower interest earnings and an additional provision taken as a result of a reduction in the estimated fair value of ABCP held by the Corporation. The above table demonstrates that for each year, the revenues generated by the GTAA were more than sufficient to cover operating expenses and interest and financing costs.

The financial results reported by the GTAA include certain non-cash items, such as amortization of capital assets, which are not included in the calculation of the aeronautical rates and charges. In accordance with its rate setting approach, the GTAA expects that revenues and reserve funds will continue to be sufficient to cover operating expenses and interest and financing costs, including notional principal. Consistent with many infrastructure developments, the GTAA's net revenues may not be sufficient to cover amortization of capital assets for a period of several years which will result in total cash and non-cash expenses exceeding revenues.

## Revenues

Revenues are derived from aeronautical charges (landing fees and general terminal charges), AIF, and non-aeronautical sources such as car parking and ground transportation, concessions, rentals, electricity sales and other sources. The primary drivers for revenue are aircraft movements and passenger activity. Landing fees are based on the MTOW and general terminal charges are based on the number of seats of an arriving aircraft. The AIF is charged per passenger and a significant portion of non-aeronautical revenues are highly correlated to passenger activity. The relationship between these revenue sources and expenses was discussed in the section on Rate Setting Approach. The following chart summarizes the GTAA's revenues for the years ended December 31, 2008, 2007 and 2006:

(in thousands)	2008	2007	2006
Landing fees	\$447,062	\$ 451,183	\$ 440,807
General terminal charges	180,674	185,027	172,453
Airport improvement fees, net	255,727	257,495	183,500
Car parking and ground transportation	126,450	114,250	102,283
Concessions and rentals	136,242	127,346	118,141
Other	26,400	27,557	45,119
	\$ 1,172,555	\$ 1,162,858	\$ 1,062,303

Total aeronautical revenue for the year ended December 31, 2008 was \$627.7 million, as compared to \$636.2 million for the year ended December 31, 2007. The decrease reflects the lowering of aeronautical rates in 2008 as compared to 2007, which more than offset the increase in activity between the two years.

AIF revenue, which is net of the commission paid to the air carriers for the collection of the AIF, decreased from \$257.5 million in 2007 to \$255.7 million in 2008. In 2007 the GTAA collected \$16.2 million in AIF related to a reconciliation of passenger volumes. Adjusted for this payment, 2008 AIF revenues increased relative to 2007 due to passenger growth in 2008.

Under the terms of the AIF agreements with the air carriers, the GTAA has committed that AIF revenue will be used primarily for capital programs at Toronto Pearson, including associated debt service (interest and principal) and reserve funds. Historically the GTAA has used AIF revenue to fund debt service,

but it retains the option of funding capital projects directly with AIF revenue. Recognizing that capital expenditures or the payment of debt service and the receipt of AIF revenue may not occur in the same period, AIF revenue earned and collected, but not used in any given period, is invested in the AIF Reserve Fund for future capital or debt service payments. In 2008, \$255.7 million of AIF revenue was earned and \$219.5 million was used for capital projects or debt service resulting in an increase in the AIF Reserve Fund. This compares to \$257.5 million earned and \$270.0 million used during 2007, with the difference in that year funded through a reduction in the AIF Reserve Fund.

The GTAA also receives fees or rental payments from car parking and ground transportation, concessions, space rental and other rental properties. In total, these categories generated \$262.7 million in revenue in 2008 as compared to \$241.6 million in revenue in 2007. This increase of 8.7% is attributable to the higher passenger volumes, which result in greater demand for parking and ground transportation services and higher sales at the various retail outlets at the Airport, as well as increased revenues from new advertising and other revenue generating initiatives. The GTAA increased vehicle parking rates in November 2007, which also affects the comparative revenues.

Other revenues decreased \$1.2 million for the year ended December 31, 2008 as compared to the same period in 2007. Other revenues primarily includes revenues from the GTAA's 117 megawatt Cogeneration Plant, which were largely unchanged in 2008 from 2007. In 2008 the GTAA changed the way it accounts for interest income. Previously certain interest income was included in other revenues. All interest income is now recorded as an offset to interest and financing costs. The 2007 results have been restated to reflect this change. However, the 2006 results included in this report have not been restated.

## **Operating Expenses**

The GTAA's operating expenses include the cost of operating and maintaining the Airport, together with interest and financing costs, and the amortization of capital assets. As noted previously, the operating expenses that are reported in the financial statements are determined according to Canadian generally accepted accounting principles and are not entirely consistent with the expenses used in the calculation of aeronautical rates and charges. Specifically, amortization is not recovered in the landing fee, while the principal component of debt service, which is not an operating expense on the financial statements, is included in the landing fee calculation.

The following chart summarizes the GTAA's operating expenses for the years ended December 31, 2008, 2007 and 2006:

(in thousands)	2008	2007	2006
Ground rent	\$140,622	\$ 149,474	\$ 147,635
Goods and services	282,188	272,722	285,894
Salaries, wages and benefits	108,571	107,139	105,090
Real property taxes and PILT	23,857	22,691	21,501
	555,238	552,026	560,120
Interest and financing costs, net	452,501	427,652	355,027
Amortization of capital costs	210,730	227,130	225,934
	\$1,218,469	\$1,206,808	\$1,141,081

The Ground Lease sets out the calculation of the annual ground rent payable by the GTAA to the federal government. In 2008 and 2009 the ground rent payable is fixed at \$141.5 million and \$138.7 million respectively. Thereafter, ground rent payable will be calculated as a percentage of the GTAA's revenues. Prior to 2008, ground rent payable was calculated based on the number of passengers using the Airport. Under Canadian generally accepted accounting principals, the ground rent expense for each of 2008 and 2009 will be recorded as the average of the fixed payments for the two years: \$140.6 million. The \$8.9 million decrease in ground rent in 2008 as compared to 2007 is a result of the new ground rent formula being used. In July 2003, the Minister of Transport announced a 24-month ground rent deferral program which had the effect of reducing the ground rent paid by \$10.0 million in 2003, \$21.0 million in 2004 and \$10.5 million in 2005. The full ground rent expense was recorded for each period, with an offsetting liability recorded on the balance sheet. However, from 2006 to 2015, as the deferred amount is paid, the amount of ground rent actually paid to the federal government will be \$4.2 million greater than the amount recorded as an expense in the financial statements with the liability reduced accordingly. The deferred amount paid each year is included in the calculation of landing fees in each year.

Goods and services, which comprise the general operating expenses for the Airport, were \$282.2 million and \$272.7 million for 2008 and 2007, respectively. In 2007 the GTAA recovered \$13.1 million of bad debts relating to Jetsgo and Canada 3000, both of which had declared bankruptcy in previous years. This amount was recorded as an offset to goods and services in 2007. When adjusted

for this recovery, 2008 goods and services expense decreased by \$3.6 million as compared to 2007. Areas where goods and services expense decreased in 2008 include a reduction in computer equipment maintenance expense, reduced expense associated with the logistics centre and the Airport Customer Assistance Program, and a reduction in bussing expense, all as a result of changes to contracts and adjustments to service levels, and a gain on the valuation of a derivative contract with the Ontario Power Authority related to the Co-generation Plant. Offsetting these savings were increased expense for snow removal related to the number of severe weather events in 2008, and increased expense for natural gas and policing.

The GTAA has both union and non-union employees and both groups are compensated with salaries and benefits, including pension plans, medical and life insurance benefits and certain other benefits. Salaries, wages and benefits increased from \$107.1 million in 2007 to \$108.6 million for 2008. The modest increase reflects salary increases for GTAA employees and an increase in pension expense, offset by a reduction in overtime expense.

The GTAA has an exemption from the payment of real property taxes under the *Assessment Act (Ontario)*, and instead pays to each of the cities of Toronto and Mississauga an amount prescribed by regulation under the Assessment Act as PILT. The amounts due are based on passenger activity for a specified prior year. PILT paid in 2007 was \$22.7 million, based on passenger activity for 2004, and PILT for 2008 was \$23.9 million based on passenger activity in 2005. Ongoing growth in passenger activity since 2005 will be reflected in higher PILT payments in future years.

The year-over-year increase in interest and financing costs is the result of the additional provision taken with respect to the fair value of ABCP held by the GTAA and lower interest income earned on reserve funds due to lower interest rates in 2008 when compared to 2007. These increases in expense were partially offset by lower bond and bank facility interest expense.

Amortization of capital assets decreased in 2008 to \$210.7 million from \$227.1 million in 2007. The GTAA uses the declining balance method to calculate depreciation of capital assets. This methodology will result in declining amortization of capital assets on a year-over-year basis absent any significant changes in the asset base.

## SUMMARY OF QUARTERLY RESULTS

Selected unaudited quarterly financial information for the period from January 1, 2007 through December 31, 2008 is set out in the following table:

(in millions)	2008				2007			
Quarter ended	Dec	Sept	June	Mar	Dec	Sept	June	Mar
Revenues	\$274	\$316	\$294	\$289	\$283	\$330	\$281	\$269
Operating expenses	142	131	130	152	147	132	127	146
Revenues over expenses <sup>1</sup>	132	185	164	137	136	198	154	123
Interest and financing, net	128	108	104	112	120	114	101	93
Amortization	55	52	52	52	57	55	56	59
Revenues over/(under) expenses	\$(51)	\$25	\$8	\$(27)	\$(41)	\$29	\$(3)	\$(29)

Note: 1. Revenues over expenses before interest and financing costs and amortization

The GTAA's quarterly results are influenced by passenger activity and aircraft movements which vary with travel demand associated with holiday periods and other factors such as weather and economic conditions. Due to these external factors the historic quarterly results cannot be relied upon for future trends. The opening of additional areas in Terminal 1 and other facilities during 2007 and in the future will impact revenues and expenses. In the fourth quarter of 2008 the GTAA increased its provision relating to its holding of ABCP from \$60.8 million to \$89.9 million. There were no other exceptional events during the fourth quarter of 2008 which had a significant impact on traffic, revenues or operating expenses.

## CAPITAL PROJECTS

After the GTAA assumed responsibility for the Airport, it initiated an extensive redevelopment program to improve and redevelop the facilities to meet current and future demand. The ADP included the construction of terminal facilities, roadways, cargo facilities, airside improvements such as runways and taxiways, ancillary services and utilities infrastructure. The ADP was designed as a demand driven program that would be undertaken while the Airport continued to operate and would provide the GTAA with some flexibility on the timing of certain stages. On January 30, 2007, with the opening of Pier F at Terminal 1, the

ADP was essentially completed. On that date all Terminal 2 operations were transferred to Terminal 1, and Terminal 2 was removed from the inventory of active facilities at the Airport. The total cost of the ADP, which was completed on time and on budget, was \$4.4 billion.

Continued long-term growth in passenger demand will necessitate further expansion of Terminal 1. In order to facilitate this eventuality, the GTAA has developed a work plan, entitled the Post ADP Program, which includes: the demolition of Terminal 2 and the Terminal 2 parking garage; apron construction in the area that Terminal 2 once occupied; replacing the Terminal 2 parking capacity and increasing the overall parking capacity at the Airport with the construction of a new parking facility in Area 6B on the east side of Airport Road; replacement of certain utilities infrastructure; and the preliminary design of Pier G at Terminal 1. This work is currently scheduled to be completed after 2012. The Post-ADP Program has an authorized budget of \$439.7 million. The final design and construction timing of Pier G and other future Airport expansion is still under review, and will be dependent on demand.

The demolition of Terminal 2 and the new apron construction was completed in 2008. Construction of the Area 6B parking facility was ongoing throughout 2008 and is expected to be completed in the fall of 2009.

In addition, the GTAA has undertaken a program to expand and redevelop certain areas in Terminal 3, including the baggage handling systems and passenger processing areas as well as other improvements. Work is ongoing in the west end of the terminal where expansions to the passenger waiting areas, baggage system and security areas are scheduled to be completed in 2009.

In 2008 the GTAA approved another capital program to improve Terminal 3. This \$85.0 million project, to be completed in 2015, will see improvements to the food and beverage and other retail offerings in the terminal and changes to passenger processing and security areas designed to improve passenger connections and other passenger flows through the terminal. There were no material expenditures on this program in 2008.

Other capital projects were undertaken during the year to upgrade, refurbish or replace existing facilities. During 2008, a total of \$33.5 million was expended on several projects including runway and taxiway repairs and upgrades totalling \$9.4 million, information technology and telecommunications based systems totalling \$7.0 million and vehicle purchases totalling \$4.6 million, with the

remainder being spent on a number of smaller maintenance and improvement projects.

The GTAA has historically funded, and expects to continue to fund, capital projects through borrowing in the debt capital markets.

## ASSETS AND LIABILITIES

Total assets and liabilities as at December 31, 2008, 2007 and 2006 are set out below:

(in millions)	2008	2007	2006
Total Assets	\$7,302.0	\$ 7,256.3	\$ 7,445.6
Total Liabilities	\$7,700.9	\$ 7,609.2	\$ 7,753.9

The increase in total assets between 2008 and 2007 reflects an increase in cash and cash equivalents and an increase in work in progress offset by a reduction in capital assets due to ongoing amortization of capital assets, and reserve funds. The increase in total liabilities between 2007 and 2008 reflects an increase in debt to fund ongoing capital work. The decrease in total assets between 2006 and 2007 reflects a decrease in reserve and other funds and a reduction in capital assets and work in progress due to ongoing amortization of capital assets. The decrease in total liabilities between 2006 and 2007 reflects debt repayments carried out in 2007.

Cash and cash equivalents increased from \$149.8 million in 2007 to \$193.9 million in 2008 as a result of the Series 2008-2 debt issue where some of the proceeds are being held for future debt repayment and capital expenditures. Total reserves and other funds as at December 31, 2008 were \$898.1 million as compared to \$907.1 million at December 31, 2007. These reserves represent funds for regular payments of interest and principal, amounts set aside with the Trustee as security for specific debt issues, funds set aside in accordance with the terms of the Trust Indenture for operating and capital expenses and funds set aside by the GTAA for future principal payments and other commitments such as the AIF Reserve Fund.

The GTAA includes in its projection of cash flow for rate setting purposes the principal amortization for each debt issue based on a 30-year amortization period for the debt, regardless of the actual term of the respective issue. Consistent with

the treatment of interest expense, principal is only included in the landing fee calculation for the debt associated with operational assets. On a quarterly basis, the GTAA funds the Notional Principal Fund with the estimated principal collected in the previous quarter. The Notional Principal Fund will be applied to the ongoing amortizing payments for Series 1999-1 revenue bonds or to repay any issue on maturity in whole or in part. On October 24, 2008 the GTAA applied the full balance of the Notional Principal Fund towards the repayment of the Series 2006-2 MTNs resulting in a zero balance in the fund at December 31, 2008, as compared to \$49.9 million at December 31, 2007.

For the AIF Reserve Fund, the GTAA accumulates AIF revenue as it is collected and uses the funds primarily for ongoing debt service payments. During 2008, the GTAA used \$219.5 million of AIF, which is the amount anticipated when setting the rates and charges for 2008. The result is that the AIF Reserve Fund increased from \$106.4 million at the end of 2007 to \$142.1 million at the end of 2008.

The primary component of total liabilities is debt, which as at December 31, 2008 totalled \$7.51 billion of current and long-term debt obligations, as compared to \$7.42 billion as at December 31, 2007. The increase represents funding for capital expenditures in 2008 and to a certain extent pre-funding of 2009 capital expenditures and debt repayments, net of 2008 debt repayments made using the Notional Principal Fund.

During 2008, the GTAA issued \$825.0 million of new debt. The 2008 MTN issues are set out in the following table:

MTN Series	Issue Date	Maturity Date	Principal	Coupon
2008-1	April 17, 2008	April 17, 2018	\$500 million	5.26%
2008-2	December 8, 2008	December 6, 2013	\$325 million	5.89%

Two debt issues were repaid in 2008: the \$375.0 million Series 2003-1 revenue bonds and the \$350.0 million Series 2006-2 floating rate MTNs.

The net deficiency reported on the balance sheet is a combination of the reserve funds which have been funded through operating revenue and cumulative revenues over or under expenses. Since revenues after operating expenses and interest and financing costs have not been sufficient to cover amortization for several operating periods, the GTAA has recorded revenues under expenses.

This has resulted in a cumulative net deficiency of \$398.9 million as at December 31, 2008 as compared to a net deficiency of \$352.9 million as at December 31, 2007. The principal component included in the aeronautical charges is based on a 30-year amortization and will therefore be lower in early years and increase over time, similar to the principal payments of a mortgage. The amortization of the GTAA's most significant assets is reported on a declining balance basis, which is higher in the early years of the asset life and decreases over time. This differential contributes to the GTAA's current net deficiency. It is anticipated that when the principal component in the landing fee increases to a level where it is equal to or exceeds the reducing amount of amortization of assets, revenue will exceed all expenses, including amortization, providing a potential improvement to the net asset position.

## **LIQUIDITY AND CAPITAL RESOURCES**

The GTAA is a non-share corporation and accordingly is funded through operating revenue, AIF revenue, reserve funds, the debt capital markets and its syndicated bank credit facility. As noted previously, aeronautical charges are set each year to cover the projected operating costs, including debt service and reserve requirements, after consideration of the projected air traffic and passenger activity and non-aeronautical revenues. Consistent with its residual approach, any funds generated by the GTAA are used to cover costs within its mandate.

An overall Capital Markets Platform was established by the GTAA with the Trust Indenture setting out the terms of all debt, including bank facilities, revenue bonds and MTNs. The program has been used to fund all capital programs and the GTAA will continue to access the debt markets to fund capital programs and to refinance some or all of its maturing debt. At December 31, 2008, there was a total of \$7.49 billion of outstanding debt issued under the Capital Markets Platform, excluding the bank facility. Any proceeds received from debt issues and not immediately required are invested in short-term investment grade debt instruments until they are required.

On February 13, 2008, the GTAA filed a new shelf prospectus qualifying up to \$2.0 billion of debt issuance for capital expenditures, reserve funds, debt refinancing and other approved uses through the 25-month period covered by the shelf prospectus.

The GTAA has a \$500 million credit facility and a \$50 million facility for interest rate and foreign exchange hedging activities, both with the same banking syndicate. These facilities mature on November 22, 2010 and can be extended annually for an additional year with the lenders' consent. Due to prevailing market conditions at the time, in 2008 the GTAA elected not to request an extension of the maturity date of the credit facilities. There was, and continues to be, no indication that the banking syndicate would not have consented to the extension had it been requested. The banking facility is used to fund capital or operating expenses, as required, and provides flexibility on the timing for accessing the capital markets in the future. This facility ranks *pari passu* with all other debt of the GTAA. As at December 31, 2008, \$2.3 million was drawn on the \$500 million facility by way of a letter of credit. No amounts were drawn against the \$50 million facility.

At December 31, 2008, the GTAA had reserve and other funds totalling \$898.1 million, which include reserve funds held by the Trustee as required by the Trust Indenture and certain funds held by the GTAA for specific or future requirements. AIF revenue collected and not used in any given year is retained in the AIF Reserve Fund for future years. The Notional Principal Fund will increase with the principal component collected in the landing fee until it is used for the repayment of debt. The other reserve funds provide additional security for the debt program.

At December 31, 2008 the GTAA held \$193.9 million of cash and cash equivalents and \$27.0 million of non-current other investments in addition to reserves and other funds.

Principal payments for the next five fiscal years include the amortizing payments for MTN Series 1999-1, and the maturity of MTN Series 2004-2, Series 2000-2, Series 2006-1, Series 2007-2, Series 2002-1, Series 2002-2 and Series 2008-2. The GTAA has also entered into certain capital leases for equipment, but the annual payments are not significant.

The next table analyzes the GTAA's financial liabilities by maturity for the next ten years based on the remaining period from December 31, 2008 to the contractual maturity date. The table has been prepared based on the contractual undiscounted cash flows based on the earliest date on which the GTAA can be required to pay. It includes both principal and interest cash flows as applicable.

(in thousands)	Less than 1 month	1 month to 12 months	1 year to 5 years	6 years to 10 years
Accounts payable and accrued liabilities	\$ 43,269	\$ 41,315	\$ -	\$ -
Province of Ontario	-	-	14,400	9,600
Long-term debt	50,400	643,873	4,294,739	2,909,181
	\$ 93,669	\$ 685,188	\$ 4,309,139	\$ 2,918,781

Accounts payable and accrued liabilities will be funded through operations while the Province of Ontario and long-term debt obligations are expected to be funded through a combination of reserve funds and debt.

In connection with the operation and development of the Airport, the GTAA had capital commitments outstanding at December 31, 2008 of approximately \$159.8 million, primarily related to construction contracts.

The objective of the GTAA's investment and cash management strategy is to ensure that the cash requirements for operations, capital programs and other demands are met and to maximize the flexibility in accessing the capital markets as may be required. The GTAA monitors its cash flow requirements accordingly. Given recent MTN issues, the credit facility, reserves and the projected operating revenues and costs, the GTAA does not anticipate any funding shortfalls in the near term. However, there may be events outside the control of the GTAA, including future impacts of the current dislocation in the credit markets, which could negatively impact its liquidity by affecting the availability and/or the cost of future borrowing.

### **Asset Backed Commercial Paper**

As at December 31, 2008, the GTAA held \$182.2 million, face value, of non-bank sponsored ABCP. Of this amount, \$130.2 million was held in reserve and other funds, and \$52.0 million, which was originally held in cash and cash equivalents, was previously reclassified to non-current other investments on the balance sheet.

At the time of purchase, all of the trusts in which the GTAA's investments in ABCP were held were rated R-1 (high) by DBRS Limited ("DBRS"), which is the highest possible rating for commercial paper and a permitted investment under the terms of the GTAA's Trust Indenture which governs the GTAA's reserve

funds. The maturity dates of the ABCP held in these and other funds ranged from August 28, 2007 to September 25, 2007; however, none were redeemed at maturity.

On December 23, 2007, the Pan-Canadian Investors Committee for Third-Party Asset Backed Commercial Paper (the "Committee") announced an agreement in principle to restructure the ABCP issued by 20 trusts, including all of the issuing trusts which issued ABCP held by the GTAA.

On March 17, 2008, the Committee filed an application in the Ontario Superior Court of Justice (the "Court") under the Companies' Creditors Arrangement Act ("CCAA") asking the Court to call a meeting of ABCP noteholders to vote on a plan of restructuring broadly in-line with the December 23, 2007 plan proposed by the Committee.

As a result of the CCAA application, on March 19, 2008, DBRS withdrew its ratings on all of the affected ABCP. As a result, the ABCP held by the GTAA no longer met the definition of qualified investments in the Trust Indenture, and as a result the GTAA was not in compliance with the requirement in the Trust Indenture that all money held in any account, fund or reserve fund established under the Trust Indenture be held in cash or invested in qualified investments. The notes that the GTAA received in January 2009 under the restructuring plan do not meet the definition of a qualified investment under the Trust Indenture by virtue of their credit rating and term to maturity. The GTAA is of the view that the non-compliance is not of a nature which would give rise to an event of default for purposes of the Trust Indenture, which requires, among other things, that any non-compliance must materially adversely affect bondholders. As of the date of this report, no event of default has occurred.

On March 20, 2008, the Committee issued an information statement containing details about the proposed restructuring. The restructuring plan was voted on and approved by the noteholders on April 25, 2008. The Court approved the restructuring on June 5, 2008. However, several noteholders appealed the Court ruling. The Ontario Court of Appeal heard this appeal on June 25 and 26, 2008 and subsequently released its ruling upholding the original Court ruling. As a result of this ruling, a group of noteholders sought leave to appeal the ruling to the Supreme Court of Canada. On September 18, 2008 the Supreme Court of Canada denied leave to appeal, resulting in the original Court approval of the restructuring remaining in place.

On December 24, 2008 the Committee reached an agreement with the governments of Canada, Quebec, Ontario and Alberta to provide an additional \$4.45 billion of margin funding by way of a senior margin funding facility. At the same time, the spread loss triggers were adjusted to reduce the likelihood that margin funding would be required and an eighteen-month moratorium on collateral calls by the asset providers to the ABCP conduits was enacted.

On December 29, 2008, DBRS assigned a provisional rating of "A" to the Class A-1 and A-2 notes to be issued under the restructuring.

Under the restructuring plan, holders of ABCP were to receive one or more type of replacement notes, depending on the underlying security of the various ABCP held:

- Traditional Asset ("TA") tracking notes which are long-term floating rate notes backed by traditional securitized assets;
- Ineligible Asset ("IA") tracking notes which are long-term floating rate notes backed by traditional securitized assets with exposure to the U.S. sub-prime mortgage market; and
- Master Asset Vehicle ("MAV") notes issued in four classes (A-1, A-2, B and C) which are long-term floating rate notes backed by a combination of leveraged collateralized debt, synthetic assets and traditional securitized assets.

Based on the restructuring plan and other public information, the GTAA estimated the fair value of its ABCP holdings as at December 31, 2008 to be \$92.3 million, approximately 50.7% of the \$182.2 million face value.

The valuation technique used by the GTAA to estimate the fair value of its investment in ABCP at December 31, 2008, incorporates probability weighted discounted cash flows derived from several possible scenarios considering the best available public information regarding market conditions and other factors that a market participant would consider for such investments. The assumptions used in determining the estimated fair value reflect the details included in the information statements issued by the Committee and the risks associated with each of the long-term floating rate notes.

Assumptions regarding the interest rates and maturities of the various long-term floating rate notes, discount rates and credit losses used in estimating the fair value include:

	Class A-1	Class A-2	Class B	Class C	TA Notes	IA Notes
Interest rate	0.98%	0.98%	0.98%	0.98%	1.91%	1.91%
Discount rate <sup>(1)</sup>	8.57%	8.82%	45%	10%	6.43%	8.82%
Approximate term	8 years	8 years	8 years	8 years	5 years	5 to 22 years
Credit loss	nil	nil	nil	nil	nil	37.5%

(1) For Class B and C Notes the indicated rate is the fair value as a per cent of face value and not the discount rate. For IA Notes the discount rate is applied after the credit provision.

Two benchmarks were utilized to determine the discount rates used in estimating the fair value of the Class A-1 and A-2 Notes as at December 31, 2008. One method used bankers' acceptance rates plus expected spreads for "A" rated financial institution debt with similar maturities. This benchmark was chosen as indicative of the market discount factor that would be applied to the restructured securities as financial institution credit spreads are at historically wide spreads relative to other similarly rated debt due to many of the same uncertainties that the restructured notes face, such as structured product and derivative exposure and counterparty risk. This benchmark was allocated a weighting of 25% in determining the discount rate. The second benchmark, weighted 75%, used to determine the appropriate discount rate, utilized the spread or premium paid on the CDX.NA.IG five-year index to determine the appropriate spread over seven year government bond rates. The CDX index was chosen in addition to the financial institution spread as it is an alternate indicator of investment grade credit market conditions and provides a second measure of investor sentiment in what continue to be uncertain markets. The five-year index was utilized as it is the most liquid index and is considered to provide a more accurate indication of market levels than the less liquid seven-year index. While the restructured notes are subject to credit enhancements such as restructured and remote margin call provisions, cross-collateralization and a dedicated margin funding facility which support an investment grade credit rating, an additional 200 and 225 basis points was added to the discount rate of the Class A-1 and Class A-2 Notes, respectively, to further reflect the uncertainties surrounding these specific instruments.

The Class B and C Notes were valued on an equity basis at 45% and 10% of face value, respectively, indicative of their subordination as to payment of both principal and interest under the restructuring proposal.

While many of the assets that will be placed in the IA Tracking Note pools continue to carry investment grade ratings, the IA Tracking Notes were given an initial credit provision of 37.5%, consistent with the default probability rates of an investment rating below "CCC". This reflects continued uncertainty surrounding the U.S. sub-prime mortgage market. Due to the substantial credit provision taken against the IA Tracking notes, the discount rate applied in the valuation methodology was determined using the approach described above and is consistent with that applied to the Class A-2 Notes. It was not considered appropriate to apply a below investment grade credit discount rate as this would effectively double count the credit provision.

The TA tracking notes were discounted at a rate consistent with current market yield on highly rated asset backed term notes with a similar term to maturity.

An increase of 1% in the weighted average discount rate would reduce the estimated fair value of the GTAA's investment in ABCP by approximately \$6.0 million.

One of the cash flow scenarios considered was a liquidation scenario whereby, if the restructuring was not successfully completed, recovery of the GTAA's investment would be through the liquidation of the underlying assets of the ABCP trusts. This scenario was assigned a probability of 2.0%. Notwithstanding final Court approval of the restructuring, due to the state of the credit markets there remained some risk as at December 31, 2008 that the restructuring could not be completed and a liquidation scenario would occur.

The probability weighted discounted cash flows resulted in an estimated fair value of the GTAA's ABCP of \$92.3 million as at December 31, 2008. This was a decrease of \$29.1 million from the September 30, 2008 estimated fair value. Therefore, the GTAA has recorded an additional impairment charge in respect of its ABCP holdings for the quarter ended December 31, 2008 of \$29.1 million. The total impairment charge recognized is approximately 49.3% of the original value.

Subsequent the end of 2008, on January 12, 2009, the Court issued the implementation order for the restructuring. The restructuring was implemented

effective January 21, 2009 and the GTAA received the following restructured notes under the plan:

- \$61.7 million MAV II Class A-1 notes, rated “A” by DBRS with an expected term to maturity of approximately 8 years
- \$59.1 million MAV II Class A-2 notes, rated “A” by DBRS with an expected term to maturity of approximately 8 years
- \$10.7 million MAV II Class B notes, which are unrated and have an expected term to maturity of approximately 8 years
- \$4.1 million MAV II Class C notes, which are unrated and have an expected term to maturity of approximately 8 years
- \$2.1 million Traditional Asset Tracking Notes in one class which are unrated and have an expected term to maturity of approximately 5 years
- \$43.1 million Ineligible Asset Tracking Notes in 4 classes which are unrated and have expected terms to maturity from 5 to 22 years.

The MAV II Class A-1 and A-2 notes and the TA and IA Tracking notes pay interest on a quarterly basis at variable interest rates. It is not expected that the MAV II Class B and C notes will pay current interest, instead interest will accrue and to the extent possible be paid after the Class A-1 and A-2 notes are repaid.

The market for these notes is currently characterized by a low volume of trades and wide bid/ask spreads. Lacking reliable market data to use in determining the fair value of the restructured notes, the GTAA estimated the fair value using a method consistent with the methodology described above.

As at January 21, 2009, the GTAA estimate of the fair value of the notes was not significantly different from the year-end value. On closing of the restructuring, the GTAA received \$6.2 million representing interest accrued on the ABCP from August 2007 to August 2008, net of restructuring costs and reserves. An additional payment representing accrued interest for the period September 2008 to the restructuring date will be paid at a later date. Due to the high degree of uncertainty regarding payment of interest on the ABCP, the full amount of this payment was not accrued in the financial statements of the GTAA in 2007 or 2008 and, accordingly, a portion of this payment will be reflected in the 2009 financial statements.

Continuing uncertainties regarding the value of the assets which underlie the restructured notes and the amount and timing of cash flows could give rise to

further material change in the fair value of the GTAA's investment in the restructured ABCP.

The GTAA has sufficient cash and other sources of liquidity available to meet its reserve requirements, and to fund its operating, capital and financing obligations, and does not expect that its operations will be materially affected by the current uncertainty over the carrying value of its restructured ABCP investments.

## **SIGNIFICANT ACCOUNTING POLICIES AND ESTIMATES**

The significant accounting policies adopted by the GTAA are set out in Notes 4 and 5 of the Financial Statements as at December 31, 2008 and 2007. In preparing the financial statements, management is required to make certain estimates or assumptions that affect the reported amount of assets and liabilities and the disclosure of commitments and contingencies at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from estimates.

The value of the ABCP held by the GTAA as at December 31, 2008 has been estimated using the methodology discussed in the section entitled Asset Backed Commercial Paper. As no reliable market currently exists for these securities this valuation estimate is subject to uncertainty and may change at subsequent reporting dates.

Property and equipment for the Airport include items such as improvements to leased land, runways, terminal and other buildings, and roadways. These assets are recorded at cost (less estimated residual value) and each asset type is amortized over the lesser of the remaining term of the Ground Lease or their estimated useful lives. Amortization of assets commences when the asset is brought into operation, and for certain assets, such as the terminal buildings, the asset may be brought into or removed from operations in stages.

The timing for revenue recognition depends on the nature of the revenue and the specific agreements in place. Landing fees, general terminal charges and car parking revenues are recognized as the airport facilities are utilized. Airport Improvement Fees, net of airline administration fees, are accrued upon the enplanement of the passenger. AIF revenues are based on passenger activity as reported by individual air carriers and may be subject to later adjustment. Concessions revenue is charged on a monthly basis and is recognized based on a

percentage of sales or specified minimum rent guarantees. Ground transportation revenue is recognized based on a combination of the duration of the term of the licences and permits and utilization fees. Rentals revenue is recognized straight-line over the duration of the respective agreements. Revenue derived from the Cogeneration Plant included in other revenue, is recognized as electricity is delivered to customers.

The GTAA maintains both defined benefit pension plans and defined contribution pension plans for its employees. The pension costs of the defined benefit plans are actuarially determined using the projected benefit method prorated on service and best estimate assumptions. For the purpose of calculating the expected return on plan assets, those assets are valued at fair value. The costs of the defined benefit plans are recognized as the benefits are earned through employee service. The costs of the defined contribution pension plans are expensed as the GTAA becomes obligated to contribute to the defined contribution plans. The assumptions used to estimate the pension plan assets and liabilities are further discussed in Note 16 of the Financial Statements of the GTAA for the years ended December 31, 2008 and 2007.

Effective January 1, 2008, the Canadian Institute of Chartered Accountants ("CICA") issued accounting standard Section 3031 – Inventories. Section 3031, which the GTAA has adopted, provides guidance on the method of determining the cost of materials and supplies. The new accounting standard specifies that inventories are to be valued at the lower of cost and net realizable value. The standard requires the reversal of previously recorded write downs to realizable value when there is clear evidence that net realizable value has increased. The adoption of Section 3031 did not materially impact the GTAA's financial statements.

### **International Financial Reporting Standards ("IFRS")**

In February 2008, the Accounting Standards Board ("AcSB") confirmed that the use of IFRS will be required in 2011 for publicly accountable enterprises in Canada. In April 2008, the AcSB issued an IFRS Omnibus Exposure Draft proposing that publicly accountable enterprises be required to apply IFRS, in full and without modification, on January 1, 2011. The transition date of January 1, 2011 will require the restatement, for comparative purposes, of amounts reported by the Corporation for its year ended December 31, 2010, and of the opening balance sheet as at January 1, 2010.

GTAA has prepared a formal conversion plan to implement IFRS which consists of three phases: scoping and diagnostic, analysis and development, and implementation and review.

Phase One has been completed which involved project planning, staffing, identification of stakeholders and documenting differences between current Canadian GAAP and IFRS. Based upon the current state of IFRS this phase has identified a small number of topics impacting the financial results of the GTAA. The International Accounting Standards Board ("IASB") has a number of activities currently underway which may change the number of topics and magnitude of the impact and as a result management will closely track the IASB's progress.

Phase Two, currently in progress, involves completion of detailed diagnostics and evaluation of the financial impacts of various options and alternative methodologies provided for under IFRS; identification and design of operational and financial business processes; and development of required solutions to address identified issues. Through this process GTAA continues to assess the financial reporting impacts of the adoption of IFRS. At this time, the impact on future financial position and results of operations cannot be reasonably determined or estimated.

Regular reporting on the plan status will be provided to the Audit Committee of the Board of Directors of GTAA as appropriate. To assist with this conversion and new disclosure requirements, an external expert advisor has been engaged.

The GTAA anticipates a significant increase in disclosure resulting from the adoption of IFRS and is continuing to assess the level of disclosure required and any necessary system changes to gather and process the information.

The GTAA will continue to execute its conversion plan and closely monitor pronouncements by the IASB that could impact financial reporting in anticipation of the 2011 changeover.

## **FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS**

In 2005, the Canadian Institute of Chartered Accountants issued three new accounting standards: Handbook Section 1530, *Comprehensive Income*, Handbook Section 3855, *Financial Instruments - Recognition and Measurement*, and Handbook

Section 3865, *Hedges*. These new standards became effective for the GTAA on January 1, 2007.

S.1530 and the guidance report entitled *Financial Instruments - Proposed New Accounting Standards - A summary for Not-for-Profit Organizations* issued by the Accounting Standards Board introduces the concept of Unrealized Changes in Net Assets ("UCNA"). UCNA represents unrealized gains and losses on financial assets classified as available-for-sale and changes in the fair value of the effective portion of cash flow hedging instruments. UCNA and the cumulative amount, Accumulated Unrealized Changes in Net Assets ("AUCNA") are presented as a category of Net Assets, in the Statements of Changes in Net Assets.

S. 3855 establishes standards for the recognition and measurement of financial assets, financial liabilities and non-financial derivatives ("financial instruments"). S. 3855 requires changes in the value of certain financial instruments to be recorded in the financial statements of a company. S. 3855 also requires that derivatives that are embedded in contracts be identified and accounted for as financial instruments. The Clean Energy Supply contract with the Ontario Power Authority associated with the Co-generation Plant contains an embedded derivative and is valued each reporting period. All financial instruments will be recognized on the balance sheet and should be measured at fair value at initial inception. The GTAA has designated its reserve funds and cash balances as available-for-sale. On December 31, 2008, the GTAA fair-valued all available-for-sale securities. Unrealized gains and losses on financial instruments designated as available-for-sale will be recognized in UCNA. Other significant accounting implications arising on the adoption of Section 3855 include the use of the effective interest method of amortization for any transaction costs or fees, premiums or discounts earned or incurred for financial instruments measured at amortized cost.

S. 3865 specifies criteria under which hedge accounting can be applied and how hedge accounting should be executed for permitted hedging strategies. As at the date of this report the GTAA is not party to any active hedges.

For the year ended December 31, 2007 the GTAA adopted new CICA standards, Section 1535 – *Capital Disclosures* and Section 3862 – *Financial Instrument Disclosure*. These standards enhance disclosure with respect to capital and financial instruments.

Reserve and other funds, other investments, accounts receivable, accounts payable and accrued liabilities and security deposits are reflected in the financial statements at values which approximate fair values because of the short-term nature of these instruments, except for ABCP which is fair-valued using the valuation technique discussed in the section entitled Asset Backed Commercial Paper.

## **INTERNAL CONTROLS AND PROCEDURES**

GTAA management is responsible for establishing and maintaining disclosure controls and procedures to ensure that information required to be disclosed to satisfy the GTAA's continuous disclosure obligations is recorded, processed, summarized and reported as required by applicable Canadian securities legislation. Management has carried out an evaluation of the effectiveness as of December 31, 2008 of the design and operation of the disclosure controls and procedures, as defined in *National Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings*, under the supervision of, and with the participation of, the President and Chief Executive Officer ("CEO"), and the Vice President and Chief Financial Officer ("CFO"). Based on this evaluation, the CEO and CFO concluded that the disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the GTAA to satisfy its continuous disclosure obligations and are effective in ensuring that information required to be disclosed in the reports that the GTAA files is accumulated and communicated to management as appropriate to allow timely decisions regarding required disclosure. The Board of Directors has reviewed and approved the GTAA's Policy Regarding Corporate Disclosure Controls and Procedures. Management has determined that as at December 31, 2008 the design and operation of the disclosure controls and procedures continues to be effective.

GTAA management is responsible for designing and implementing internal controls over financial reporting to provide reasonable assurance regarding the reliability of the Corporation's reporting and the preparation of financial statements for external purposes in accordance with Canadian generally accepted accounting principles. As required under *National Instrument 52-109*, the GTAA, under the supervision and with the participation of the CEO and the CFO, has carried out an evaluation of the effectiveness as at December 31, 2008 of its internal controls over financial reporting. Based on this evaluation, the GTAA's CEO and CFO concluded that the Corporation maintained effective

internal control over financial reporting as at December 31, 2008. While no material weaknesses with respect to internal controls over financial reporting were identified during the assessment, such assessment may not detect all weaknesses nor prevent or detect all misstatements because of inherent limitations. Additionally, projections of any assessment of effectiveness to future periods are subject to the risk that controls may become inadequate due to changes in conditions or deterioration in the degree of compliance with the Corporation's policies and procedures. There were no changes in the GTAA's internal control over financial reporting that occurred during the quarter ended December 31, 2008 that have materially affected, or are reasonably likely to materially affect, its internal control over financial reporting.

## **RISKS AND UNCERTAINTIES**

The GTAA experienced continued growth in total passenger volumes in 2008. However, during the fourth quarter of 2008 there was a 1.7% reduction in passenger volume compared to the fourth quarter of 2007. The risk of sudden and possibly significant impacts or volatility in air travel demand due to external sources such as economic conditions, geopolitical unrest, terrorism, government regulation, world health epidemics and the financial uncertainty in the aviation industry, continue to exist. Any of these could impact the GTAA's financial results. Due to current economic conditions the GTAA anticipates that passenger demand and aeronautical activity will decline in 2009 when compared to 2008 levels. It is expected that the decrease in 2009 passenger volumes will have a negative impact on the GTAA's revenues. The GTAA has prepared and is executing a contingency plan based on the decline in passengers and aeronautical activity. The contingency plan includes cost reduction measures, the postponement of capital projects, an increase to the Airport Improvement Fee and the implementation of an air service rebate program that offers rebates on landing fees to air carriers who introduce new routes to the Airport or increase their aircraft capacity on existing routes serving the Airport.

In 2003, Toronto experienced an outbreak of Severe Acute Respiratory Syndrome ("SARS"), and, more recently, there has been extensive commentary on the potential of a pandemic or severe outbreak of avian flu. Depending on the location, timing, and extent of an outbreak of a highly contagious illness such as SARS or avian flu, there could be significant impacts on regional or world travel. The GTAA has worked with Health Canada to understand the risks of such an event, and has developed operational contingency plans based on various scenarios.

Subsequent to the Air France incident on August 2, 2005, the GTAA, together with other parties, was named as a defendant in a class action lawsuit and other separate lawsuits commenced by certain passengers and by Air France. The GTAA's insurers are defending this action and it is the opinion of the GTAA that this is an insurable event. Consequently, it is expected that the GTAA's financial exposure, if any, will be limited to its insurance deductibles. This event also demonstrates that there are always operational risks associated with an airport. The GTAA mitigates these risks through strict compliance with safety requirements and regulations and emergency response procedures.

The financial stability of the aviation industry remains a risk for the GTAA, particularly with respect to domestic air carriers. To date the GTAA has not experienced any losses directly due to foreign air carriers filing for bankruptcy protection. However, the GTAA has incurred losses due to Canadian airlines seeking creditor protection or declaring bankruptcy. There is some risk to aviation activity and revenues from industry changes or exposure to a dominant air carrier. This risk is increased during periods of economic uncertainty. However, this risk is mitigated by the fact that approximately 75% of the passenger activity at the Airport originates or terminates at Toronto Pearson.

Although overall passenger traffic at Pearson Airport increased by 2.8% in 2008 compared to 2007, it became evident during the latter part of 2008 that passenger volumes were declining as the economic slowdown in the United States spread to Canada and the rest of the world. The airlines responded in a number of ways to reduce their aircraft and seat capacity. In some cases, less profitable routes were cancelled or reduced in frequency. Some air carriers have allocated smaller aircraft to lower volume North American routes while at the same time some air carriers have been substituting larger aircraft on high volume and long haul international routes and adjusting their frequencies to ensure high load factors. Such changes in the fleet mix and air service patterns can impact the GTAA's planning of facilities and traffic for projecting future landing fees and general terminal charges. The GTAA uses projected revenues, expenses, MTOW and arrived seats to calculate the landing fee per tonne and the general terminal charge per seat. The risks inherent in this approach are that expenses may be underestimated or non-aeronautical revenues overestimated, resulting in inadequate aeronautical revenue for the GTAA to break even on a modified cash basis or meet its debt covenants. Aeronautical revenue may also be lower than expected if there is a reduction in the number of movements or the size of aircraft as compared to projections.

While the ADP was substantially completed with the opening of Pier F in January 2007, the GTAA continues to undertake capital projects as required to maintain the Airport and meet air travel demand. Capital projects are subject to risks relating to costs, schedule and other events.

There is always risk when raising funds in the capital markets, including risks relating to fluctuations in interest rates, and the availability of funds at any point in time. External factors such as economic conditions, government policies, catastrophic events and the state of the financial markets can impact the GTAA's ability to access the capital markets. While the GTAA debt program has historically been well received by the capital markets in Canada, the current dislocation in the global capital markets could affect the GTAA's ability to meet its financing requirements. The GTAA monitors the overall debt markets and works with its financial advisors to select the timing, size and term of any debt issue to ensure continued access to the markets and to maximize opportunities. The GTAA also monitors its debt maturity profile to minimize refinancing risk in the future.

As part of the debt program, the Trust Indenture sets out certain covenants that the GTAA must meet, including two specific coverage tests for operating expenses and debt service payments. If revenue or expenses are substantially different than projected, there is a risk of not meeting the coverage tests. The operating covenant states that the total revenue must at least cover all operating expenses, including interest and financing costs. The debt service covenant states that the net revenues, which may include available credit, must be at least 1.25 times the total interest and financing costs, including notional principal. In meeting these tests, the AIF revenue included is the amount transferred from the AIF Reserve Fund, and may not be the same as the AIF earned. If the debt service covenant test is not met in any year, the GTAA is not in default of its obligations under the Trust Indenture so long as the test is met in the subsequent year.

Since the GTAA and CAW Local 2002 which represents the unionized employees of the GTAA (not including firefighters) were unable to agree on the terms of a consolidated collective agreement, the parties are scheduled to appear before the Canadian Industrial Relations Board in May 2009. If the CIRB instructs the parties to re-engage in negotiations and the negotiations reach an impasse, then a conciliator will be appointed to assist the parties to reach a settlement. If the conciliation fails, then mandatory mediation will occur during which time, the CAW may issue a strike notice or the GTAA may issue a lockout notice. Prior to

either notice being given, an Essential Services Agreement would be agreed to by the parties or imposed on the parties by the CIRB. The Essential Services Agreement would identify unionized employees who would be unable to strike or be locked out so as to ensure the health and safety of the workplace and the safeguarding of passengers. It is anticipated that the primary impact of a strike or lockout of GTAA's unionized employees would be delays in accessing the Airport due to picketing activity.

In addition, there is the possibility of a strike by the unionized employees of Air Canada, whose collective agreements will expire in June 2009. It is anticipated that a strike or lockout of Air Canada's unionized employees could result in delays in accessing the Airport due to picketing activity, and could result in a decrease in the GTAA's revenues if Air Canada's operations are materially impacted. In the event of a strike by the unionized employees of the GTAA or Air Canada, the GTAA will implement its labour contingency plans to maintain airport operations.

Due to the nature of its operations and the magnitude of the ADP and other capital projects, the GTAA is exposed to litigation risk from time to time. The GTAA manages its litigation risk primarily through its Corporate Risk and Legal Services Departments, its claims settlement processes and insurance.

The litigation where GTAA is a defendant fall into three categories: those covered by insurance, construction claims and other litigation. Litigation covered by insurance are personal injury and property damage claims, including the ten lawsuits arising from the Air France accident of August 2, 2005, where the GTAA's financial exposure is limited to its insurance deductible.

The GTAA is defending four construction claims in various stages of litigation or settlement discussions.

Other litigation includes an application by the City of Mississauga ("Mississauga") to review a decision by Public Works and Government Services Canada which determined that the GTAA was required to pay Mississauga \$841,360 in payments in lieu of development charges regarding Airport development undertaken by the GTAA between 1996 and 2004. Mississauga seeks additional payments in lieu of development charges of \$26 million.

Where appropriate, the GTAA has recorded provisions or reserves while it actively pursues its position with respect to litigation. Where it is the opinion of

management that the ultimate outcome of these matters will not have a material effect upon the GTAA's financial position, results of operations, or cash flows, no reserves have been recorded.

The availability of adequate insurance coverage is subject to the conditions of the overall insurance markets and the GTAA's claims and performance record. The GTAA has continued to be successful in placing all of its insurance needs.

## **CONCLUSION**

While 2008 saw continued growth in Airport activity, the latter part of the year was characterized by slowing growth, and in the fourth quarter, declining passenger activity when compared to the same period in 2007. The GTAA expects 2009 to be marked by a decline in passenger volumes and aeronautical activity when compared to 2008. The GTAA is closely monitoring aviation activity in order to respond to any changes in activity beyond that which is anticipated. In 2008 continued focus on initiatives to generate non-aeronautical revenue and to control costs resulted in financial performance that exceeded the GTAA's original expectations for the year. The GTAA's five-year strategic plan is intended to further develop revenue, efficiency and customer service initiatives.

The GTAA is at a point in its development where the Airport has sufficient capacity to meet demand for several years. As a result, the demand for new capital development funds is greatly reduced from the period when the ADP was being implemented. This pause in the redevelopment of the Airport, together with the management focus expressed in the strategic plan, position the GTAA well to continue to meet the developing air travel needs of the Southern Ontario region.

## **CAUTION REGARDING FORWARD-LOOKING INFORMATION**

This MD&A contains certain forward-looking information about the GTAA. This forward-looking information is based on a variety of assumptions and is subject to risks and uncertainties. There is significant risk that predictions, forecasts, conclusions and projections, which constitute forward-looking information, will not prove to be accurate, that the assumptions may not be correct and that actual results may vary from the forward-looking information. The GTAA cautions readers of this MD&A not to place undue reliance on the forward-looking information as a number of factors could cause actual results, conditions, actions

or events to differ materially from the targets, expectations, estimates or intentions expressed in the forward-looking information.

Words such as “believe”, “expect”, “plan”, “intend”, “estimate”, “anticipate” and similar expressions, as well as future or conditional verbs such as “will”, “should”, “would” and “could” often identify forward-looking information. Specific forward-looking information in this MD&A includes, among others, statements regarding: future demand for air travel in the GTA; budgets and expenditures relating to capital programs; future capital development at the Airport; the GTAA’s annual debt capital requirements; the relationship between the GTAA’s revenues and reserve funds, and its operating expenses and interest and financing costs; non-aeronautical revenues; airline load factors and fleet mixes; the GTAA’s liquidity; the GTAA’s ability to continue to meet the increasing air travel needs of the Southern Ontario region; the estimated fair value of the GTAA’s restructured ABCP holdings; continuing uncertainties regarding the value of the assets which underlie the restructured ABCP and the amount and timing of cash flows derived from the restructured ABCP; the possibility of further material changes in the value of the GTAA’s restructured ABCP holdings; and the effect of the current uncertainty regarding the GTAA’s restructured ABCP investments on its liquidity and operations.

This forward-looking information is based on a variety of material factors and assumptions including, but not limited to: long-term growth in population, employment and personal income will provide the basis for long-term increased aviation demand in the GTA; the Canadian and U.S. economies will perform at expected levels in the near term; air carrier capacity will meet demand for air travel in the GTA; the growth and sustainability of low fare and other air carriers will contribute to long-term aviation demand in the GTA; economic and air travel industry factors will result in a short-term decline in air travel at the Airport; domestic, transborder and international travel will exhibit long-term growth; the commercial aviation industry will not be directly affected by terrorism; the cost of enhancing aviation security will not overly burden air carriers or the GTAA; no significant event will occur which impacts the ordinary course of business such as a natural disaster or other calamity; and the GTAA will be able to access the capital markets at competitive terms and rates. These assumptions are based on information currently available to the GTAA, including information obtained by the GTAA from third-party experts and analysts.

Risk factors that could cause actual results to differ materially from the results expressed or implied by forward-looking information include, among other things: levels of aviation activity; air carrier instability; aviation liability insurance; fuel prices; construction risk; geographical unrest; terrorist attacks; war; health epidemics, labour negotiations; capital market and economic conditions; changes in laws; adverse regulatory developments or proceedings; lawsuits; and other risks detailed from time to time in the GTAA's publicly filed disclosure documents.

The forward-looking information contained in this MD&A represents the GTAA's expectations as of the date of this report and is subject to change. Except as required by applicable law, the GTAA disclaims any intention or obligation to update or revise any forward-looking information included in this MD&A whether as a result of new information, future events or for any other reason.

**Financial Statements of the  
Greater Toronto Airports Authority**

**December 31, 2008 and 2007**



# Greater Toronto Airports Authority

## Balance Sheet

As at December 31 (in thousands)	2008	2007
<b>Assets</b>		
Current		
Cash and cash equivalents	\$ 193,911	\$ 149,822
Accounts receivable (Note 8)	45,677	54,594
Prepaid expenses	3,430	2,864
Inventory	8,843	7,397
	<b>251,861</b>	<b>214,677</b>
Reserve and other funds (Note 6)	898,096	907,120
Other investments (Note 7)	27,040	28,802
Other assets (Note 10)	70,387	69,687
Property and equipment (Note 11)	5,690,769	5,847,182
Work in progress (Note 12)	340,411	176,559
Accrued benefit asset (Note 16)	23,395	12,265
	<b>\$ 7,301,959</b>	<b>\$ 7,256,292</b>
<b>Liabilities</b>		
Current		
Bank indebtedness	\$ 1,036	\$ -
Accounts payable and accrued liabilities	84,584	77,678
Security deposits and deferred credits	36,374	36,363
Current portion of deferred ground rent (Note 3)	4,156	4,156
Current portion of long-term debt (Note 13)	362,993	836,228
	<b>489,143</b>	<b>954,425</b>
Deferred credit (Note 10)	37,619	39,822
Deferred ground rent (Note 3)	24,938	29,094
Long-term debt (Note 13)	7,149,180	6,585,811
	<b>7,700,880</b>	<b>7,609,152</b>
<b>Net Assets (Deficiency) (Note 22)</b>		
Externally restricted	72,579	72,857
Internally restricted	261,932	284,728
Unrestricted	(733,432)	(710,445)
	<b>(398,921)</b>	<b>(352,860)</b>
	<b>\$ 7,301,959</b>	<b>\$ 7,256,292</b>

Commitments and contingent liabilities (Note 19 and 20)

Signed on behalf of the Board:

\_\_\_\_\_  
Marilynne E. Day-Linton, Director

\_\_\_\_\_  
Lawrence D. Worrall, Director

# Greater Toronto Airports Authority

## Statement of Operations

Years Ended December 31 (in thousands)	2008	2007
<b>Revenues</b>		
Landing fees	\$ 447,062	\$ 451,183
General terminal charges	180,674	185,027
Airport improvement fees, net (Note 9)	255,727	257,495
Car parking and ground transportation	126,450	114,250
Concessions	80,187	72,232
Rentals	56,055	55,114
Other	26,400	27,557
	<b>1,172,555</b>	<b>1,162,858</b>
<b>Operating Expenses</b>		
Ground rent (Note 3)	140,622	149,474
Goods and services	282,188	272,722
Salaries, wages and benefits	108,571	107,139
Real property taxes and payments-in-lieu of real property taxes (Note 17)	23,857	22,691
	<b>555,238</b>	<b>552,026</b>
Revenues over expenses before interest and financing costs and amortization	617,317	610,832
Interest and financing costs, net (Notes 6 and 15)	452,501	427,652
Amortization of property and equipment	210,730	227,130
Revenues under expenses	\$ (45,914)	\$ (43,950)

# Greater Toronto Airports Authority

## Statement of Net Assets

2008						
Year Ended December 31 (in thousands)	Balance, Beginning of Year	Unrealized Changes in Net Assets	Revenues Under Expenses	Transfers/ Allocations and Other	Use of Funds	Balance, End of Year
<b>Externally restricted</b>						
Operating and maintenance reserve	\$ 61,175	\$ -	\$ -	\$ (10,876)	\$ -	\$ 50,299
Renewal and replacement reserve	3,000	-	-	-	-	3,000
Debt service fund - principal	8,682	-	-	33,912	(23,314)	19,280
	72,857	-	-	23,036	(23,314)	72,579
<b>Internally restricted</b>						
Airport improvement fees collected, net	106,387	-	-	255,225	(219,500)	142,112
Notional principal of long-term debt	49,878	-	-	90,000	(139,878)	-
Debt service coverage requirement	128,463	-	-	(8,643)	-	119,820
	284,728	-	-	336,582	(359,378)	261,932
<b>Total Restricted net assets</b>	<b>357,585</b>	<b>-</b>	<b>-</b>	<b>359,618</b>	<b>(382,692)</b>	<b>334,511</b>
<b>Unrestricted</b>						
Unrestricted net deficiency	(713,154)	-	(45,914)	23,074	-	(735,994)
Accumulated unrealized changes in net assets:						
Loss on hedge	(8,659)	922	-	-	-	(7,737)
Gain on interest rate swap	11,368	(1,069)	-	-	-	10,299
<b>Unrestricted net deficiency</b>	<b>(710,445)</b>	<b>(147)</b>	<b>(45,914)</b>	<b>23,074</b>	<b>-</b>	<b>(733,432)</b>
<b>Total Net deficiency</b>	<b>\$ (352,860)</b>	<b>\$ (147)</b>	<b>\$ (45,914)</b>	<b>\$ 382,692</b>	<b>\$ (382,692)</b>	<b>\$ (398,921)</b>
<b>2007</b>						
Year Ended December 31 (in thousands)	Balance, Beginning of Year	Unrealized Changes in Net Assets	Revenues Under Expenses	Transfers/ Allocations and Other	Use of Funds	Balance, End of Year
<b>Externally restricted</b>						
Operating and maintenance reserve	\$ 64,524	\$ -	\$ -	\$ (3,349)	\$ -	\$ 61,175
Renewal and replacement reserve	3,000	-	-	-	-	3,000
Debt service fund - principal	17,135	-	-	17,087	(25,540)	8,682
	84,659	-	-	13,738	(25,540)	72,857
<b>Internally restricted</b>						
Airport improvement fees collected, net	119,114	-	-	257,273	(270,000)	106,387
Notional principal of long-term debt	218,275	-	-	118,800	(287,197)	49,878
Debt service coverage requirement	85,923	-	-	42,540	-	128,463
	423,312	-	-	418,613	(557,197)	284,728
<b>Total Restricted net assets</b>	<b>507,971</b>	<b>-</b>	<b>-</b>	<b>432,351</b>	<b>(582,737)</b>	<b>357,585</b>
<b>Unrestricted</b>						
Unrestricted net deficiency	(819,590)	-	(43,950)	150,386	-	(713,154)
Accumulated unrealized changes in net assets:						
Loss on hedge	(9,581)	922	-	-	-	(8,659)
Gain on interest rate swap	12,437	(1,069)	-	-	-	11,368
<b>Unrestricted net deficiency</b>	<b>(816,734)</b>	<b>(147)</b>	<b>(43,950)</b>	<b>150,386</b>	<b>-</b>	<b>(710,445)</b>
<b>Total Net deficiency</b>	<b>\$ (308,763)</b>	<b>\$ (147)</b>	<b>\$ (43,950)</b>	<b>\$ 582,737</b>	<b>\$ (582,737)</b>	<b>\$ (352,860)</b>

## Greater Toronto Airports Authority

### Statement of Cash Flows

Years Ended December 31 (in thousands)	2008	2007
<b>Cash Flows from Operating Activities</b>		
Revenues under expenses	\$ (45,914)	\$ (43,950)
Items not affecting cash		
Amortization of property and equipment	210,730	227,130
Writedown of reserve and other funds and other investments (Notes 6 and 7)	52,700	37,200
Loss on disposal of property and equipment	1,128	3,680
Amortization of other assets	1,210	1,207
Excess of cash funding over pension expense	(11,130)	(1,788)
Change in fair value of derivative, net	(1,910)	409
Changes in non-cash working capital		
Decrease in accounts receivable	8,917	37,236
(Increase) Decrease in prepaid expenses	(566)	712
Increase in inventory	(1,446)	(1,162)
Increase in accounts payable, accrued liabilities and accrued interest	6,147	4,072
(Decrease) Increase in security deposits and deferred credits	(2,192)	26,865
	<b>217,674</b>	<b>291,611</b>
<b>Cash Flows from Investing Activities</b>		
Acquisition of property and equipment	(2,694)	(6,429)
Proceeds on disposal of property and equipment	194	920
Work in progress (Note 12)	(210,775)	(218,973)
Land acquisition costs and other assets (Note 10)	-	(14,034)
Other investments (Note 7)	(10,826)	(37,000)
Reserve and other funds	(31,088)	149,504
	<b>(255,189)</b>	<b>(126,012)</b>
<b>Cash Flows from Financing Activities</b>		
Issuance of medium term notes and long-term debt (Note 13)	821,741	800,849
Repayment of medium term notes and long-term debt (Note 13)	(736,626)	(895,957)
Draw on credit facility	400,609	-
Repayment of credit facility	(401,000)	-
Bank indebtedness	1,036	-
Decrease in deferred ground rent payable (Note 3)	(4,156)	(4,156)
	<b>81,604</b>	<b>(99,264)</b>
<b>Net Cash Inflow</b>	<b>44,089</b>	<b>66,335</b>
<b>Cash and Cash Equivalents, Beginning of Year</b>	<b>149,822</b>	<b>83,487</b>
<b>Cash and Cash Equivalents, End of Year</b>	<b>\$ 193,911</b>	<b>\$ 149,822</b>

As at December 31, 2008, cash and cash equivalents consisted of short-term investments of \$193.9 million, cash of \$10.5 million less outstanding cheques of \$11.5 million. At December 31, 2007, cash and cash equivalents consisted of short-term investments of \$146.8 million, cash of \$15.2 million less outstanding cheques of \$12.2 million (see Note 24, Comparative figures).

## 1. National Airports Policy

In July 1994, the federal government announced its National Airports Policy whereby the management, operation and maintenance of 26 airports within the National Airport System was to be transferred through various ground lease arrangements to locally controlled Canadian Airport Authorities (“CAAs”). The National Airports Policy also prescribed the Fundamental Principles for the Creation and Operation of CAAs including the Public Accountability Principles to be adopted by each CAA.

CAAs are free to operate airports on a commercial basis and have the authority to set all fees and charges. The federal government retains regulatory control over aeronautics and as such will set safety and security standards for airports, licence airports and regulate the aviation industry as a whole.

## 2. Corporate Profile of the Greater Toronto Airports Authority

Greater Toronto Airports Authority (“GTAA”) was incorporated on March 3, 1993 under Part II of the *Canada Corporations Act*, as a corporation without share capital. This corporate structure ensures that the excess of revenues over expenses is retained and reinvested in airports and airport operations under control of the GTAA. The Bylaws of the GTAA were amended in 1994 to conform with the requirements of the National Airports Policy. The GTAA has all the powers, obligations and duties of any private Canadian corporation. The GTAA is governed by a 15-member Board of Directors (the “Board”). Directors serve a term of three years and are eligible to be re-appointed subject to a maximum limit of nine years. Five Directors are appointed from municipal candidates. Each of the Regional Municipalities of York, Halton, Peel and Durham and the City of Toronto are entitled to provide, on a rotating basis, the names of three candidates and the Board appoints one of the three candidates for each available position as a Director. In addition, four Directors are appointed by the Board on a cyclical basis on the basis of candidates nominated by a pool of nominators comprised of the Law Society of Upper Canada, the Association of Professional Engineers of Ontario, the Institute of Chartered Accountants of Ontario, the Toronto Board of Trade and the Boards of Trade and Chambers of Commerce in the Regional Municipality of York, the Regional Municipality of Halton, the Regional Municipality of Durham and the Regional Municipality of Peel. Finally, the Government of Canada and the Province of Ontario are entitled to appoint two Directors and one Director, respectively, while the Board of Directors is entitled to appoint three Directors.

The mandate of the GTAA is to operate and develop a regional network of airports in the Greater Toronto Area (“GTA”). Under the terms of a ground lease (see Note 3, Airport subject to ground lease), the first airport in this network, Toronto Pearson International Airport (the “Airport”), was transferred to the GTAA in 1996. The Airport’s operations

## **2. Corporate Profile of the Greater Toronto Airports Authority (continued)**

on 1,867 hectares of land include Terminals 1 and 3, airside assets including five runways, taxiways and aprons, groundside assets including bridges and parking lots, infield assets including an aircraft deicing facility and cargo buildings, and ancillary structures. Excluded are any assets owned by Nav Canada, the operator of Canada's civil air navigation system.

The GTAA is committed to the continuing development of the Airport. This includes continued redevelopment of the terminals, increasing airside capacity to six runways, increasing cargo and aircraft facilities, and reconstructing the roadway system.

## **3. Airport Subject to Ground Lease**

On December 2, 1996, the GTAA assumed the operation, management and control of the Airport for a period of 60 years, together with one renewal term of 20 years, by virtue of a ground lease (the "Ground Lease") between the GTAA, as tenant, and Her Majesty the Queen in Right of Canada, represented by the Minister of Transport ("Transport Canada"), as landlord. The GTAA assumed the obligations of Transport Canada under all existing agreements at the Airport.

The Ground Lease is the principal document governing the relationship between the GTAA and Transport Canada at the Airport. It determines the rent to be paid and generally allocates risk and responsibilities between the GTAA and the federal government for all matters related to the operation of the Airport. Under the Ground Lease, all revenue and expenditure contracts in effect on December 1, 1996 were assigned to the GTAA. The GTAA did not assume any liability with respect to claims against the federal government incurred prior to December 2, 1996.

By virtue of its status as the tenant under the Ground Lease, the GTAA has the authority to set and collect airline rates and charges, negotiate and issue leases, licences and permits and construct and develop the infrastructure of the Airport. The Ground Lease permits the GTAA to pledge its leasehold interest in the Airport as security.

On February 11, 2008, the GTAA executed an amendment to the Ground Lease which replaces the previous calculation that was largely based on passenger traffic with one that is based on revenue. The new formula will be phased in such that in 2008 and 2009 ground rent will be at fixed amounts. Beginning in 2010, ground rent will be calculated as a percentage of revenue using an escalating percentage of Airport Revenue which has the following ranges: 0% for revenue below \$5.0 million, 1% for revenue between \$5.0 million and \$10.0 million, 5% for revenue between \$10.0 million and \$25.0 million, 8% for revenue between \$25.0 million and \$100.0 million, 10% for revenue between \$100.0 million and \$250.0 million, and 12% for revenue in excess of \$250.0 million. The GTAA will continue to be required to repay ground rent deferred in the 2003 to 2005 period.

### **3. Airport Subject to Ground Lease (continued)**

In July 2003, the Government of Canada announced a program to allow for a deferral in the ground rent for a two-year period commencing July 1, 2003, in the amount of \$41.6 million. This amount is being repaid over a 10-year period, commencing in 2006, through increased annual ground rent payments of approximately \$4.2 million per year. The decrease in the liability for 2008 was approximately \$4.2 million, bringing the total remaining liability to \$29.1 million.

### **4. Significant Accounting Policies**

#### **Presentation and Basis of Accounting**

The GTAA's financial statements are prepared in accordance with Canadian generally accepted accounting principles. The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of commitments and contingencies at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. These estimations and assumptions include the useful lives of property and equipment, valuation allowances and certain revenue amounts. Actual results could differ from estimates.

#### **Ground Lease**

The Ground Lease is accounted for as an operating lease.

#### **Cash and Cash Equivalents**

Cash and cash equivalents include cash and short-term, highly liquid investments with an original term of 90 days or less.

#### **Inventory**

Inventory consists of natural gas and parts and supplies held for use at the Airport. Inventory is stated at the lower of cost and net realizable value.

#### **Other Assets**

As required under the terms of the Ground Lease, the title of any land acquired is transferred to the federal government while GTAA retains use of the land. The purchase price for acquired land is recorded as land acquisition costs and amortized on a straight-line basis over the remaining term of the Ground Lease.

## 4. Significant Accounting Policies (continued)

### Acquisitions

Assets acquired related to the development of the Airport are capitalized to work in progress or property and equipment. Costs related to projects under construction are capitalized until the construction project or replacement facilities become operational.

### Property and Equipment

Property and equipment are recorded at cost. Property and equipment include items such as improvements to leased land, runways, buildings and roadways. These assets will revert to Transport Canada upon the expiration or termination of the Ground Lease. No assets are amortized longer than the current expiry date of the Ground Lease.

The costs of property and equipment (less estimated residual values) are amortized over the lesser of the remaining term of the Ground Lease or their estimated useful lives. Property and equipment are amortized at the following annual rates:

<b>Terminal Assets</b>	
Buildings and support facilities, parking structures, pedestrian bridges and approach systems, and apron works	2.5% declining balance for terminal facilities 2.5% to 20% declining balance for non-terminal facilities
Baggage handling systems	Straight-line over 25 years
<b>Airside Assets</b>	
Improvements to leased land	Straight-line over remaining term of the Ground Lease
Runways and taxiways	2.5% declining balance 15 years straight-line for runway and taxiway surfaces
Deicing facilities	2.5% declining balance
<b>Other Assets</b>	
Utilities and stormwater management facilities	2.5% declining balance
Operating assets	10% to 30% declining balance
Capital leases	10% to 30% declining balance

Leases entered into by the GTAA for the use or operation of equipment are classified as capital, to the extent they meet the criteria for capitalization in accordance with generally accepted accounting principles.

## **4. Significant Accounting Policies (continued)**

### **Work in Progress**

Work in progress is transferred to property and equipment when the asset is placed in service. Interest associated with borrowing funds for work in progress is capitalized until the work is substantially complete and assets are operational.

### **Revenue Recognition**

Landing fees, general terminal charges and car parking revenues are recognized as the airport facilities are utilized. Airport improvement fees, net of airline administration fees, are accrued upon the enplanement of the passenger and are subject to reconciliation with the air carriers (see Note 9, Airport improvement fees). Concessions revenue is charged on a monthly basis and is recognized based on a percentage of sales or specified minimum rent guarantees. Ground transportation revenue is recognized based on a combination of the duration of the term of the licences and permits and utilization fees. Rentals revenue is recognized straight-line over the duration of the respective agreements. Revenue derived from the Cogeneration facility, included in other revenue, is recognized as electricity is delivered to customers.

### **Salaries, Wages and Benefits**

Reimbursements from certain service organizations for salaries, wages and benefits have been included in this operating expense category. Employee benefits are accrued as earned by employees.

### **Employee Future Benefit Plans**

The GTAA maintains both defined benefit pension plans and defined contribution pension plans for its employees. The pension costs of the defined benefit plans are actuarially determined using the projected benefit method prorated on service and best estimate assumptions. For the purpose of calculating the expected return on plan assets, those assets are valued at fair value. The unamortized net actuarial gain or loss exceeding 10% of the greater of the accrued benefit obligation at the beginning of the year and the fair value of plan assets at the beginning of the year is deferred and amortized over the average remaining service life of active employees. The average remaining service period of the active employees covered by one of the defined benefit pension plans is eight years (2007 – eight years) and the other plan is two years (2007 – four years). Past service costs arising from plan amendments are deferred and amortized on a straight-line basis over the average remaining service period of active employees at the date of amendment. The

#### **4. Significant Accounting Policies (continued)**

costs of the defined benefit plans are recognized as the benefits are earned through employee service. The costs of the defined contribution pension plans are expensed as the GTAA becomes obligated to contribute to the defined contribution plans.

##### **Deferred Financing Costs**

Deferred financing costs are included in the debt balances and recognized as an adjustment to interest expense over the life of the debt. The GTAA uses the effective interest method to recognize bond interest expense, where the amount to be recognized varies over the life of the debt based on the principal outstanding.

##### **Derivative Financial Instruments**

Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. The method of recognizing the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the items being hedged.

Derivative financial instruments, including interest rate swaps and foreign exchange hedges, may be used from time to time to reduce exposure to fluctuations in interest rates and foreign exchange rates. Payments and receipts under interest rate swap agreements will be recognized as adjustments to interest and financing costs where the underlying instrument is a GTAA debt issue and as adjustments to interest income where the underlying instrument is an investment. Derivative financial instruments that are not designated by the GTAA to be in an effective hedging relationship will be carried at fair value with the changes in fair value, including any payments and receipts made or received, being recorded in interest and financing costs.

Currently, the GTAA has no derivative instruments outstanding that have been designated as hedges. However, certain accumulated unrealized changes in net assets relating to discontinued cash flow hedges are being amortized into income over the term to maturity of the related hedged item.

##### **Financial Instruments**

Financial assets and financial liabilities are initially recognized at fair value and their subsequent measurement is dependant on their classification as described below.

Their classification depends on the purpose for which the financial instruments were acquired or issued, their characteristics and the GTAA's designation of such instruments.

All financial assets must be classified either as held-for-trading ("HFT"), available-for-sale ("AFS"), held-to-maturity ("HTM"), or loans and receivables. All financial liabilities must be classified as either HTM or other liabilities ("OL"). Subsequent to initial recognition, the standards require that all financial assets and financial liabilities,

#### 4. Significant Accounting Policies (continued)

including all derivatives, be measured at fair value with the exception of loans and receivables, securities classified as HTM, liabilities classified as OL.

Any changes in unrealized gains or losses related to AFS securities that are considered temporary and certain unrealized gains and losses relating to cash flow hedging activities are disclosed as separate components of Accumulated unrealized changes in net assets.

##### Classification of Financial Instruments

The following is a summary of the accounting model the GTAA has applied to each of its significant categories of financial instruments:

Cash and cash equivalents	Available-for-sale
Accounts receivable	Loans and receivables
Reserve and other funds	Available-for-sale
Other investments	Available-for-sale
Derivative	Held-for-trading
Accounts payable and accrued liabilities	Other liabilities
Security deposits	Other liabilities
Long-term debt	Other liabilities

##### Held-for-Trading

HFT financial assets are financial assets typically acquired for resale prior to maturity. They are measured at fair value at the balance sheet date. Interest earned, interest accrued, gains and losses realized on disposal and unrealized gains and losses from market fluctuations are included in the statement of operations.

##### Loans and Receivables

Loans and receivables are accounted for at amortized cost.

##### Available-for-Sale

AFS financial assets are those non-derivative financial assets that are designated as AFS, or that are not classified as loans and receivables, HTM investments or HFT. AFS financial assets are carried at fair value with unrealized gains and losses that are considered temporary are included in unrealized changes in net assets until realized when the cumulative gain or loss is transferred to interest and financing costs or if the assets become impaired on an other than temporary basis.

#### **4. Significant Accounting Policies (continued)**

##### **Other liabilities**

OL are recorded at amortized cost and include all liabilities other than derivatives to which the fair value has been applied.

#### **5. Change in Accounting Standard**

Effective January 1, 2008, the Canadian Institute of Chartered Accountants (“CICA”) issued accounting standard Section 3031 – *Inventories*. Section 3031 provides guidance on the method of determining the cost of materials and supplies. The new accounting standard specifies that inventories are to be valued at the lower of cost and net realizable value. The standard requires the reversal of previously recorded write downs to realizable value when there is clear evidence that net realizable value has increased. The adoption of Section 3031 did not materially impact the GTAA’s financial statements.

## 6. Reserve and Other Funds

The Debt Service Fund and Debt Service Reserve Fund (the "Trust Funds") and Operations, Capital and Financing Funds invested in cash and other investments are as follows:

(in thousands)	2008	2007
<b>Debt Service Fund</b>		
Interest	\$ 99,019	\$ 96,203
Principal	19,280	8,682
	<b>118,299</b>	<b>104,885</b>
<b>Debt Service Reserve Fund</b>		
Revenue Bonds		
Series 1997-3 due December 3, 2027	37,840	36,863
Series 1999-1 due July 30, 2029	41,178	40,001
<b>Medium Term Notes</b>		
Series 2000-1 due June 12, 2030	40,000	38,623
Series 2000-2 due July 19, 2010	23,123	32,037
Series 2001-1 due June 4, 2031	36,213	35,226
Series 2002-1 due January 30, 2012	31,948	31,120
Series 2002-2 due December 13, 2012	30,402	29,615
Series 2002-3 due October 15, 2032	39,493	38,270
Series 2003-1 due June 2, 2008	-	19,389
Series 2004-1 due February 2, 2034	39,870	38,790
Series 2004-2 due February 4, 2009	11,426	11,148
Series 2005-1 due June 1, 2015	18,287	17,584
Series 2005-3 due February 15, 2016	16,881	16,471
Series 2006-1 due February 28, 2011	11,270	11,000
Series 2006-2 due October 24, 2008	-	12,329
Series 2007-1 due June 1, 2017	22,432	21,848
Series 2007-2 due May 14, 2010	8,255	12,943
Series 2008-1 due April 17, 2018	26,672	-
Series 2008-2 due December 6, 2013	19,194	-
	<b>454,484</b>	<b>443,257</b>
<b>Bank indebtedness secured by Series 1997 - A Bond</b>	<b>10,082</b>	<b>10,075</b>
	<b>464,566</b>	<b>453,332</b>
<b>Operations, Capital and Financing Funds</b>		
Operating and Maintenance Reserve Fund	50,299	61,175
Renewal and Replacement Reserve Fund	3,000	3,000
Airport Improvement Fee Reserve Fund	142,112	106,387
Notional Principal Fund	-	49,878
Debt Service Coverage Fund	119,820	128,463
	<b>315,231</b>	<b>348,903</b>
	<b>\$ 898,096</b>	<b>\$ 907,120</b>

## 6. Reserve and Other Funds (continued)

### (a) Asset Backed Commercial Paper:

As at December 31, 2008, the GTAA held \$182.2 million (2007 - \$182.2 million), face value, of non-bank sponsored ABCP. Of this amount, \$130.2 million (2007 - \$145.2 million) was held in reserve and other funds and \$52.0 million (2007 - \$37.0 million) was held in other investments (see Note 7, Other investments) on the balance sheet.

At the time of purchase, all of the trusts in which the GTAA's investments in ABCP were held were rated R-1 (high) by DBRS Limited ("DBRS"), which is the highest possible rating for commercial paper and a permitted investment under the terms of the GTAA's Trust Indenture which governs the GTAA's reserve funds. The maturity dates of the ABCP held in these and other funds ranged from August 28, 2007, to September 25, 2007; however, none were redeemed at maturity.

On December 23, 2007, the Pan-Canadian Investors Committee for Third-Party Asset Backed Commercial Paper (the "Committee") announced an agreement in principle to restructure the ABCP issued by 20 trusts, including all of the issuing trusts which issued ABCP held by the GTAA.

On March 17, 2008, the Committee filed an application in the Ontario Superior Court of Justice (the "Court") under the Companies' Creditors Arrangement Act ("CCAA") asking the Court to call a meeting of ABCP noteholders to vote on a plan of restructuring broadly in-line with the December 23, 2007 plan proposed by the Committee.

As a result of the CCAA application, on March 19, 2008, DBRS withdrew its ratings on all of the affected ABCP. As a result, the ABCP held by the GTAA no longer met the definition of qualified investments in the Trust Indenture, and as a result the GTAA was not in compliance with the requirement in the Trust Indenture that all money held in any account, fund or reserve fund established under the Trust Indenture be held in cash or invested in qualified investments. The newly restructured notes that the GTAA received in January 2009 under the restructuring plan also do not meet the definition of a qualified investment under the Trust Indenture by virtue of their credit rating and term to maturity (see Note 23, Subsequent events). The GTAA is of the view that the non-compliance is not of a nature which would give rise to an event of default for purposes of the Trust Indenture, which requires, among other things, that any non-compliance must materially adversely affect bondholders. As of the date of this report, no event of default has occurred.

On March 20, 2008, the Committee issued an information statement containing details about the proposed restructuring. The restructuring plan was voted on and approved by the noteholders on April 25, 2008. The Court approved the restructuring on June 5, 2008; however, several noteholders appealed the Court ruling. The Ontario Court of Appeal

## 6. Reserve and Other Funds (continued)

heard this appeal on June 25 and 26, 2008 and subsequently released its ruling upholding the original Court ruling. As a result of this ruling, a group of noteholders sought leave to appeal the ruling to the Supreme Court of Canada. On September 18, 2008 the Supreme Court of Canada denied leave to appeal, resulting in the original Court approval of the restructuring remaining in place.

On December 24, 2008, the Committee reached an agreement with the governments of Canada, Quebec, Ontario and Alberta to provide an additional \$4.5 billion of margin funding by way of a senior margin funding facility. At the same time, the spread loss triggers were adjusted to reduce the likelihood that margin funding would be required and an eighteen-month moratorium on collateral calls by the asset providers to the ABCP conduits was enacted.

On December 29, 2008, DBRS assigned a provisional rating of "A" to the Class A-1 and A-2 notes to be issued under the restructuring.

Under the restructuring plan, holders of ABCP are to receive one or more types of replacement notes, depending on the underlying security of the various ABCP held:

- Traditional Asset ("TA") tracking notes which are long-term floating rate notes backed by traditional securitized assets;
- Ineligible Asset ("IA") tracking notes which are long-term floating rate notes backed by traditional securitized assets with exposure to the U.S. sub-prime mortgage market; and
- Master Asset Vehicle ("MAV") notes issued in four classes (A-1, A-2, B and C) which are long-term floating rate notes backed by a combination of leveraged collateralized debt, synthetic assets and traditional securitized assets.

Based on the restructuring plan and other public information, the GTAA estimated the fair value of its ABCP holdings held in reserve and other funds and other investments (see Note 7, Other investments) as at December 31, 2008 to be \$92.3 million (2007 - \$145.0 million), approximately 50.7% (2007 - 79.6%) of the original \$182.2 million face value, resulting in a cumulative impairment of \$89.9 million (2007 - \$37.2 million).

The valuation technique used by the GTAA to estimate the fair value of its investment in ABCP at December 31, 2008, incorporates probability weighted discounted cash flows derived from several possible scenarios considering the best available public information regarding market conditions and other factors that a market participant would consider for such investments. The assumptions used in determining the estimated fair value reflect the details included in the information statements issued by the Committee and the risks associated with each of the long-term floating rate notes. Assumptions regarding the interest rates and maturities of the various long-term floating rate notes, discount rates and credit losses used in estimating the fair value include:

## 6. Reserve and Other Funds (continued)

	Class A-1	Class A-2	Class B	Class C	TA Notes	IA Notes
Interest rate	0.98%	0.98%	0.98%	0.98%	1.91%	1.91%
Discount rate <sup>(1)</sup>	8.57%	8.82%	45.00%	10.00%	6.43%	8.82%
Approximate term	8 years	8 years	8 years	8 years	5 years	5 to 22 years
Credit loss	nil	nil	nil	nil	nil	37.5%

(1) For Class B and C Notes the indicated rate is the fair value as a per cent of face value and not the discount rate. For IA Notes the discount rate is applied after the credit provision.

Two benchmarks were utilized to determine the discount rates used in estimating the fair value of the Class A-1 and A-2 Notes as at December 31, 2008. One method used bankers' acceptance rates plus expected spreads for "A" rated financial institution debt with similar maturities. This benchmark was chosen as indicative of the market discount factor that would be applied to the restructured securities as financial institution credit spreads are at historically wide spreads relative to other similarly rated debt due to many of the same uncertainties that the restructured notes face, such as structured products and derivative exposures and counterparty risks. This benchmark was allocated a weighting of 25% in determining the discount rate. The second benchmark, weighted 75%, used to determine the appropriate discount rate utilized the spread or premium paid on the CDX.NA.IG five-year index to determine the appropriate spread over seven-year government bond rates. The CDX index was chosen in addition to the financial institution spread as it is an alternate indicator of investment grade credit market conditions and provides a second measure of investor sentiment in what continue to be uncertain markets. The five-year index was utilized as it is the most liquid index and is considered to provide a more accurate indication of market levels than the less liquid seven-year index. While the restructured notes are subject to credit enhancements such as restructured and remote margin call provisions, cross-collateralization and a dedicated margin funding facility which support an investment grade credit rating, an additional 200 and 225 basis points were added to the discount rate of the Class A-1 and Class A-2 Notes, respectively, to further reflect the uncertainties surrounding the liquidity of these instruments. The prior year financial statements did not incorporate the CDX index in the valuation methodology as disruptions in credit markets resulted in low liquidity and high levels of volatility in the index which the GTAA believes at the time, made it a poor indicator in assessing the fair value of the restructured notes.

The Class B and C Notes were valued on an equity basis at 45% and 10% of face value, respectively, indicative of their subordination as to payment of both principal and interest under the restructuring proposal.

## 6. Reserve and Other Funds (continued)

While many of the assets that will be placed in the IA Tracking Note pools continue to carry investment grade ratings, the IA Tracking Notes were given an initial credit provision of 37.5%, consistent with the default probability rates of an investment rating below "CCC". This reflects continued uncertainty surrounding the U.S. sub-prime mortgage market. Due to the substantial credit provision taken against the IA Tracking notes, the discount rate applied in the valuation methodology was determined using the approach described above and is consistent with that applied to the Class A-2 Notes. It was not considered appropriate to apply a below investment grade credit discount rate as this would effectively double count the credit provision.

The TA tracking notes were discounted at a rate consistent with current market yield on highly rated asset backed term notes with a similar term to maturity.

An increase of 1% in the weighted average discount rate would reduce the estimated fair value of the GTAA's investment in ABCP by approximately \$6.0 million (2007 - \$6.8 million).

One of the cash flow scenarios considered was a liquidation scenario whereby, if the restructuring was not successfully completed, recovery of the GTAA's investment would be through the liquidation of the underlying assets of the ABCP trusts. This scenario was assigned a probability of 2.0%. Notwithstanding final Court approval of the restructuring, due to the state of the credit markets there remained some risk as at December 31, 2008 that the restructuring would not be completed and a liquidation scenario would occur.

The probability weighted discounted cash flows resulted in an estimated fair value of the GTAA's ABCP of \$92.3 million (2007 - \$145.0 million) as at December 31, 2008. This was a decrease of \$29.1 million from the September 30, 2008 estimated fair value due to the continued turmoil in the credit markets and the lack of liquidity of these investments. Therefore, the GTAA has recorded an additional impairment charge in respect of its ABCP holdings for the quarter ended December 31, 2008, of \$29.1 million. The total impairment charge recognized is approximately 49.3% of the original value.

On January 12, 2009, the Court issued the implementation order for the restructuring (see Note 23, Subsequent events).

Continuing uncertainties regarding the value of the assets which underlie the ABCP, the amount and timing of cash flows and the outcome of the restructuring process could give rise to further material change in the fair value of the GTAA's investment in ABCP.

The GTAA has sufficient cash and other sources of liquidity available to meet its reserve requirements, and to fund its operating, capital and financing obligations, and does not expect that its operations will be materially affected by the current uncertainty over the fair value of its ABCP investments.

## 6. Reserve and Other Funds (continued)

(b) Components of Reserve Funds:

### Trust Funds

The GTAA is required to establish and maintain with the Trustee the Trust Funds in accordance with the terms of the Trust Indenture (see Note 13, Credit facility and long-term debt). The Trust Funds are held for the benefit of the bondholders and noteholders for use and application by the Trustee in accordance with the terms of the Trust Indenture.

(i) Debt Service Fund (principal and interest)

Amounts in the Debt Service Fund are allocated to either an Interest Account or a Principal Account. On a monthly basis, the GTAA is required to deposit into the Interest Account an amount equal to one-sixth of the semi-annual aggregate interest requirement due on all outstanding bonds and medium term notes. Also on a monthly basis, the GTAA is required to deposit into the Principal Account an amount equal to one-twelfth of the total principal amount included in annual debt service, during the term, for any bonds or notes due in such year. The principal requirements of the Debt Service Fund were funded from the Notional Principal Fund during 2008 and has a balance of \$19.3 million at December 31, 2008 (2007 - \$8.7 million). Amounts in the Debt Service Fund are held by the Trustee for the benefit of the bondholders or noteholders and are disbursed by the Trustee to pay interest and principal as it becomes due.

Principal of \$23.3 million was paid from the Debt Service Fund in 2008 (2007 - \$25.5 million). During 2008, \$33.9 million was deposited and/or allocated to the Principal Account of the Debt Service Fund by the GTAA for the principal of the Series 1999-1, Series 2003-1, Series 2006-2 and Series 2004-2 bonds (2007 - \$17.1 million). The deposit to the Principal Account of the Debt Service Fund to fulfill principal requirements was funded from the Notional Principal Fund (see Operations, Capital and Financing Funds below) during the year.

(ii) Debt Service Reserve Fund

To the extent provided in any Supplemental Indenture, the GTAA is required to set aside funds in the Debt Service Reserve Fund for each series of bonds or medium term notes. The required amount is established at the time of issue of each series of bonds or medium term notes and funded from the proceeds of each issue. Amounts held in the Debt Service Reserve Fund are held by the Trustee for the benefit of the bondholders or noteholders for use and application in accordance with the terms of the Trust Indenture. At the maturity of each series of bonds or medium term notes, funds not applied by the Trustee will be returned to the GTAA.

## **6. Reserve and Other Funds (continued)**

### **Operations, Capital and Financing Funds**

The GTAA has established an Operating and Maintenance Reserve Fund and a Renewal and Replacement Reserve Fund pursuant to the Trust Indenture. The Operating and Maintenance Reserve Fund is equal to one-sixth of the projected operating and maintenance expenses for the following fiscal year. As at December 31, 2008 this fund had a balance of \$50.3 million (2007 - \$61.2 million). This amount is to be used only for operating and maintenance expenses or other purposes as required for the safe, ongoing operation and maintenance of the Airport as set out in the Trust Indenture. The Renewal and Replacement Reserve Fund of \$3.0 million (2007 - \$3.0 million) is to be used for unanticipated repairs to, or the replacement of, property and equipment as set out in the Trust Indenture.

In conjunction with the airport improvement fee agreements with participating airlines, the GTAA has established an Airport Improvement Fee Reserve Fund for the deposit of fees collected and not yet utilized. As at December 31, 2008, this fund had an accumulated balance of \$142.1 million (2007 - \$106.4 million). During 2008, \$219.5 million (2007 - \$270.0 million) of accumulated Airport Improvement Fee Funds were utilized for some debt service payments.

Capital and financing funds include Notional Principal and Debt Service Coverage Funds, which are amounts that have been collected through airline rates and charges. The Notional Principal Fund may be used to reduce future debt obligations, when principal is due for any series of bonds or medium term notes. For non-amortizing debt, principal is deemed to be included in annual debt service, based on a 30-year amortization, commencing on the same date as interest is expensed. The Debt Service Coverage Fund is established to meet the coverage requirements set out in the Trust Indenture, and as at December 31, 2008 had a balance of \$119.8 million (2007 - \$128.5 million).

## **7. Other Investments**

At December 31, 2008, the GTAA held \$52.0 million (2007 - \$37.0 million), face value, of ABCP investments classified as other investments. In 2008, \$15.0 million, face value of ABCP investments previously held in reserve and other funds were allocated to other investments. The estimated fair value of these investments at the time of transfer was \$10.8 million. In 2008, the GTAA also recognized an additional \$12.6 million fair value impairment in respect of these ABCP holdings (2007 - \$8.2 million) and charged that balance to interest and financing costs in the statement of operations (see Note 6, Reserve and other funds). The total impairment charge recognized is approximately 48.1 % of the original value.

## 8. Accounts Receivable

(in thousands)	2008	2007
Trade accounts receivable	\$ 40,762	\$ 50,663
Less: allowance for doubtful accounts	(701)	(881)
Trade accounts receivable, net	40,061	49,782
Other receivables	5,616	4,812
	<b>45,677</b>	<b>54,594</b>
Less: non-current portion	-	-
Total accounts receivable	\$ 45,677	\$ 54,594

The fair values of accounts receivables approximate their book values as at December 31, 2008.

There are no balances due from related parties.

Before accepting a new customer, the GTAA uses an external credit scoring system to assess the potential customer's credit quality as well as an internal credit rating system. The GTAA performs a detailed review of accounts on a customer by customer basis when assessing impairments. Each account is assessed based on factors surrounding the credit risk of specific customers including historical trends, the influence of the current economic environment and other information.

New customers are subject to credit checks and, depending on their perceived credit risk, may require prepayment or a deposit in the form of cash or a letter of credit. A security deposit is required for all non-aeronautical customers. As such, the allowance for doubtful accounts is specific in nature. No amount is subject to write-off until all possible collection action has been taken by the GTAA.

Interest is charged on all overdue balances at a rate of prime plus 3% per annum unless otherwise stipulated in terms agreed upon by both parties of the contract.

As of December 31, 2008, accounts receivable of \$1.1 million (2007 - \$1.4 million) were considered past due but not considered impaired. These amounts relate to a number of customers with no recent history of default. The aging of these receivables past due at December 31, 2008 and 2007 are as follows:

(in thousands)	2008	2007
1 to 5 days	\$ 3	\$ 447
6 to 15 days	92	300
16 to 30 days	621	582
31 to 60 days	157	39
61+ days	261	8
Total balance past due	\$ 1,134	\$ 1,376

## 8. Accounts Receivable (continued)

As of December 31, 2008, total accounts receivable of \$0.7 million (2007 - \$1.0 million) were considered impaired and not included in the table above. A provision of \$0.7 million (2007 - \$0.9 million) has been made against these related impaired accounts receivable balances.

These impaired receivables mainly relate to customers where collection is uncertain or amounts are being disputed by the GTAA's customers.

Movements in the allowance for doubtful accounts are as follows:

(in thousands)	2008	2007
Balance, beginning of year	\$ 881	\$ 17,229
Provision for new doubtful accounts	(41)	725
Amounts written off during the period	(139)	(3,982)
Amounts recovered during the period	-	(13,091)
Balance, end of year	\$ 701	\$ 881

Bad debt expense (recovery) has been included in goods and services expense in the statement of operations. Amounts included in the provision account are generally written off when there is no expectation of recovering amounts owing.

## 9. Airport Improvement Fees

Airport improvement fees ("AIF") reported in the statement of operations are recorded net of airline administration charges of \$10.5 million during 2008 (2007 - \$10.6 million).

AIF revenue is remitted to the GTAA based on airlines self-assessing their passenger counts. In 2007, as a result of completing the annual reconciliation process with air carriers, the GTAA recorded an increase of \$16.2 million in net AIF revenue.

## 10. Other Assets

(in thousands)	December 31, 2008		
	Cost	Accumulated Amortization	Net Book Value
Deferred leasehold inducements	\$ 6,107	\$ 1,908	\$ 4,199
Land acquisition costs	26,139	1,152	24,987
	\$ 32,246	\$ 3,060	\$ 29,186
Fair value of the OPA derivative			41,201
			\$ 70,387

(in thousands)	December 31, 2007		
	Cost	Accumulated Amortization	Net Book Value
Deferred leasehold inducements	\$ 6,107	\$ 1,219	\$ 4,888
Land acquisition costs	26,139	631	25,508
	\$ 32,246	\$ 1,850	\$ 30,396
Fair value of the OPA derivative			39,291
			\$ 69,687

The aggregate amortization expense in respect of other assets for the year ended December 31, 2008 was \$1.2 million (2007 - \$1.2 million) and is included in goods and services expense. There were no additions to other assets during the year (2007 - \$56.6 million).

On February 1, 2006, the GTAA entered into a Clean Energy Supply contract ("CES Contract") with the Ontario Power Authority ("OPA"), pursuant to which the GTAA is obligated to have 90 MW of electrical energy available to the Ontario power grid. The term of the CES Contract is for 20 years, subject to early termination rights available to the GTAA. The contract allows for payments by either party, depending on whether net electricity market revenues that the GTAA is deemed to have earned are greater or less than a predetermined threshold, as defined in the CES Contract.

The contract has been determined to be a derivative to be carried at fair value and upon adoption of the new financial instrument standards in 2007, the derivative was fair valued at \$39.7 million. The fair value of the derivative as at December 31, 2008 was \$41.2 million. The GTAA realized an increase in the fair value of the derivative during the year of \$7.0 million which was recorded in goods and services expense, and received cash proceeds of approximately \$5.1 million which reduced its carrying value.

The GTAA also recorded a deferred credit of \$42.0 million which is being amortized over the term of 20 years. The unamortized balance at December 31, 2008 was \$37.6 million (2007 - \$39.8 million).

## 11. Property and Equipment

Property and equipment are comprised of:

(in thousands)	December 31, 2008		
	Cost	Accumulated Amortization	Net Book Value
<b>Terminal Assets</b>			
Buildings and support facilities, parking structures, pedestrian bridges and approach systems and apron works	\$ 5,184,503	\$ 613,749	\$ 4,570,754
Baggage handling systems	276,466	52,903	223,563
	5,460,969	666,652	4,794,317
<b>Airside Assets</b>			
Improvements to leased land	9,480	1,889	7,591
Runways and taxiways	392,258	48,541	343,717
Deicing facilities	29,906	6,418	23,488
	431,644	56,848	374,796
<b>Other Assets</b>			
Utilities and stormwater management facilities	345,597	50,798	294,799
Operating assets	614,562	389,546	225,016
Capital leases	10,001	8,160	1,841
	970,160	448,504	521,656
	\$ 6,862,773	\$ 1,172,004	\$ 5,690,769

(in thousands)	December 31, 2007		
	Cost	Accumulated Amortization	Net Book Value
<b>Terminal Assets</b>			
Buildings and support facilities, parking structures, pedestrian bridges and approach systems and apron works	\$ 5,173,809	\$ 492,199	\$ 4,681,610
Baggage handling systems	276,053	41,827	234,226
	5,449,862	534,026	4,915,836
<b>Airside Assets</b>			
Improvements to leased land	9,480	1,731	7,749
Runways and taxiways	383,431	41,349	342,082
Deicing facilities	29,906	5,813	24,093
	422,817	48,893	373,924
<b>Other Assets</b>			
Utilities and stormwater management facilities	342,003	40,901	301,102
Operating assets	589,682	336,740	252,942
Capital leases	11,329	7,951	3,378
	943,014	385,592	557,422
	\$ 6,815,693	\$ 968,511	\$ 5,847,182

## 12. Work in Progress

(in thousands)	Beginning of Year	Additions/ Adjustments	Transfers to Property and Equipment	End of Year
Terminal Development Project	\$ 96,388	\$ 179,340	\$ (13,728)	\$ 262,000
Restoration Projects	40,502	26,402	(32,283)	34,621
T3 Redevelopment	39,669	13,732	(9,611)	43,790
	\$ 176,559	\$ 219,474	\$ (55,622)	\$ 340,411

As at December 31, 2008, work in progress included capitalized interest and financing costs in the amount of \$27.6 million (2007 – \$16.6 million).

## 13. Credit Facility and Long-Term Debt

During 2008, the GTAA redeemed the 2003-1 medium term note with a face value of \$375.0 million and the 2006-2 medium term note with a face value of \$350.0 million for total gross repayments of \$725.0 million. In addition, during the year the GTAA issued the 2008-1 medium term note with a face value of \$500.0 million and the 2008-2 medium term note with a face value of \$325.0 million for total gross proceeds of \$825.0 million.

As at December 31, 2008, long-term debt including accrued interest and net of unamortized discounts and premiums consists of:

### 13. Credit Facility and Long-Term Debt (continued)

(in thousands)	Coupon	Maturity	Principal	2008	2007
Series	Rate	Date	Amount		
Revenue Bonds, <i>See below</i>					
1997-3	6.45%	December 3, 2027	\$ 375,000	\$ 371,538	\$ 371,404
1999-1	6.45%	July 30, 2029	455,030	463,198	473,363
Medium Term Notes					
2000-1	7.05%	June 12, 2030	550,000	550,046	550,019
2000-2	6.70%	July 19, 2010	600,000	619,470	619,965
2001-1	7.10%	June 4, 2031	500,000	497,776	497,698
2002-1	6.25%	January 30, 2012	500,000	512,167	511,859
2002-2	6.25%	December 13, 2012	475,000	474,730	474,364
2002-3	6.98%	October 15, 2032	550,000	558,257	558,270
2003-1	5.17%	June 2, 2008	-	-	375,762
2004-1	6.47%	February 2, 2034	600,000	609,377	609,285
2004-2	4.45%	February 4, 2009	250,000	254,451	253,734
2005-1	5.00%	June 1, 2015	350,000	348,138	347,763
2005-3	4.70%	February 15, 2016	350,000	354,164	353,990
2006-1	4.40%	February 28, 2011	250,000	252,013	251,269
2006-2, <i>See below</i>	floating	October 24, 2008	-	-	352,875
2007-1	4.85%	June 1, 2017	450,000	448,902	448,719
2007-2, <i>See below</i>	floating	May 14, 2010	350,000	350,649	351,178
2008-1	5.26%	April 17, 2018	500,000	502,767	-
2008-2	5.89%	December 6, 2013	325,000	324,159	-
				7,491,802	7,401,517
Capital Leases				1,296	2,527
Province of Ontario					
Interest-free loan, payable in five equal annual installments commencing 2011					
				19,075	17,995
				7,512,173	7,422,039
Less current portion (including accrued interest)					
				362,993	836,228
				\$ 7,149,180	\$ 6,585,811

Interest expense from the GTAA's debt instruments amounted to \$426.3 million (2007 - \$432.9 million) net of capitalized interest of \$14.7 million (2007 \$16.6 million). Cash paid during 2008 for interest amounted to \$435.1 million (2007 - \$443.4 million).

### 13. Credit Facility and Long-Term Debt (continued)

For Series 2006-2 and 2007-2, interest rates are adjusted quarterly at the three-month Bankers' Acceptance rate plus 14 basis points and 11 basis points respectively. For Series 2006-2 interest rates ranged from 3.36% to 4.90% (2007 – 4.49% to 4.90%). For Series 2007-2 interest rates ranged from 2.11% to 4.82% (2007 – 4.48% to 4.96%).

With the exception of Series 1999-1 revenue bonds, principal on each series of revenue bonds and medium term notes is payable on the maturity date. Series 1999-1 are amortizing revenue bonds repayable in scheduled annual installments of principal, payable on July 30 of each year. These payments commenced July 30, 2004 and continue until maturity.

Set out below is a comparison of the amounts that would be reported if long-term debt amounts were reported at fair values. Fair values were based on quoted market rates for GTAA bonds as at December 31, 2008:

(in thousands)	2008		2007	
	Book Value	Fair Value	Book Value	Fair Value
Long-term debt	\$ 7,512,173	\$ 7,301,950	\$ 7,422,039	\$ 7,948,433

With the exception of Series 2007-2, interest is payable semi-annually from the Interest Payable Commencement Date, based on fixed rates. For Series 2007-2, interest is payable quarterly from the Interest Payable Commencement Date, based on floating rates.

With the exception of Series 2004-2, Series 2006-1, and Series 2007-2 medium term notes, which are not redeemable, the notes are redeemable in whole or in part at the option of the GTAA at any time at a redemption price based on yields over Government of Canada bonds with similar terms to maturity.

#### Credit Facility

The GTAA maintains a credit facility with a syndicate of six Canadian banks. The credit facility is secured by a \$550.0 million pledge bond (Series 1997-A) issued pursuant to the Trust Indenture. Indebtedness under the credit facility ranks *pari passu* with other indebtedness issued under the Trust Indenture. Under this credit facility, the GTAA is provided with a \$500.0 million facility for general corporate purposes and capital expenditures, and a \$50.0 million facility for interest rate and foreign exchange hedging activities. This facility matures on November 22, 2010 and can be extended annually for an additional year with the lenders' consent.

As at December 31, 2008, \$2.25 million was drawn on the \$500.0 million facility by way of a letter of credit (2007 - \$2.25 million) (see Note 19, Commitments and contingent

### 13. Credit Facility and Long-Term Debt (continued)

liabilities). No amounts were drawn against the \$50.0 million facility (2007 – nil). Indebtedness under the credit facility bears interest at rates that vary with the lenders' prime rate, Bankers' Acceptance rates and LIBOR, as appropriate. If funds were drawn on the facility in the year, interest rates would have ranged from 1.97% to 6.00% (2007 – 4.69% to 6.25%).

### 14. Leases

#### Capital Leases

The GTAA leases certain equipment as part of its operations. All leases are on a fixed repayment basis and no arrangements have been entered into for contingent rental payments.

Amounts payable under these capital leases are as follows:

(in thousands)	Minimum Lease		Present Value of	
	Payments		Minimum Lease	
	2008	2007	2008	2007
Within one year	\$ 838	\$ 1,434	\$ 802	\$ 1,350
In the second to fifth years, inclusive	517	1,235	494	1,177
	<b>1,355</b>	<b>2,669</b>	<b>1,296</b>	<b>2,527</b>
Less: future finance charges	(59)	(142)	-	-
Present value of minimum lease payments	<b>\$ 1,296</b>	<b>\$ 2,527</b>	<b>\$ 1,296</b>	<b>\$ 2,527</b>
Included in the balance sheet as:				
Current liabilities			\$ 802	\$ 1,350
Long-term debt			494	1,177
			<b>\$ 1,296</b>	<b>\$ 2,527</b>

As at December 31, 2008, the effective interest rates of the capital leases range from 0.00% to 7.81% (2007 - 0.00% to 7.93%).

#### Operating Leases

The future minimum lease payments under non-cancellable operating leases, excluding payments under the Ground Lease (see Note 19, Commitments and contingent liabilities) are as follows:

## 14. Leases (continued)

(in thousands)	
2009	\$ 5,884
2010	740
	\$ 6,624

## 15. Interest and Financing Costs, Net

Interest and financing costs for long-term debt and bank facilities, net of interest earned on the Debt Service Reserve Fund, reserves and other funds and capitalized interest is as follows:

(in thousands)	2008	2007
Interest and financing costs incurred	\$ 495,179	\$ 489,996
Less:		
Interest earned on the Debt Service Reserve Fund	(15,768)	(25,253)
Interest earned on Reserves and other funds	(12,203)	(20,499)
Capitalized interest	(14,707)	(16,592)
	\$ 452,501	\$ 427,652

Included in interest and financing costs incurred is a \$52.7 million fair value impairment (2007 - \$37.2 million) in respect of the GTAA's ABCP holdings (see Note 7, Other investments).

## 16. Employee Benefits

### Defined Benefit Pension Plans

The GTAA maintains three defined benefit pension plans. One of these plans is for former Transport Canada employees who were eligible to elect to transfer their pension credits to the GTAA plan.

The GTAA measures its accrued benefit obligations and the fair value of plan assets for accounting purposes as at December 31<sup>st</sup> of each year. The most recent actuarial valuation of the pension plans for funding purposes was as of January 1, 2008 and the next required valuation will be as of January 1, 2009.

Aggregate information about the GTAA's defined benefit pension plans as at December 31 is as follows:

## 16. Employee Benefits (continued)

(in thousands)	2008	2007
<b>Accrued Benefit Obligation</b>		
Balance, beginning of year	\$ 103,586	\$ 97,626
Actuarial gain	(31,331)	(1,823)
Current service cost	3,556	3,330
Interest cost	5,858	5,279
Benefits paid	(2,256)	(1,794)
Employee contributions	765	968
Balance, end of year	80,178	103,586
<b>Plan Assets</b>		
Fair value, beginning of year	105,789	99,991
Employee contributions	765	968
Employer contributions	14,728	4,692
Actual return on plan assets	(16,657)	1,932
Benefits paid	(2,256)	(1,794)
Fair value, end of year	102,369	105,789
Funded status - surplus	22,191	2,203
Unamortized net actuarial loss	834	9,400
Unamortized past service costs	270	543
Unamortized transitional obligation	100	119
<b>Accrued Benefit Asset</b>	<b>\$ 23,395</b>	<b>\$ 12,265</b>

As at December 31, 2008, each of the GTAA's defined benefit pension plans were in a surplus position. One plan was in a surplus position of \$16.3 million (2007 - \$1.4 million deficit), with an accrued obligation of \$69.0 million (2007 - \$91.6 million) and a fair value of plan assets of \$85.3 million (2007 - \$90.2 million). The other plan was in a surplus position of \$5.9 million (2007 - \$3.6 million surplus), with an accrued obligation of \$11.2 million (2007 - \$12.0 million) and a fair value of plan assets of \$17.1 million (2007 - \$15.6 million).

In 2008, the Office of the Superintendent of Financial Institutions ("OSFI") determined that the actuarial valuation reports filed by the GTAA from January 1, 2004 to January 1, 2008 which recommended an employer contribution holiday was inconsistent with the Regulations to the Pension Benefits Standards Act. Pursuant to subsequent correspondence with OSFI, the amount of an additional contribution was determined resulting in a \$7.4 million contribution made by the GTAA in December 2008.

## 16. Employee Benefits (continued)

The GTAA's net defined benefit pension plan expense is as follows:

(in thousands)	2008	2007
Current service cost	\$ 3,556	\$ 3,330
Interest cost	5,858	5,279
Actual return on plan assets	16,657	(1,932)
Actuarial gain	(31,331)	(1,823)
Costs arising in the period	(5,260)	4,854
Difference between costs arising in the period and costs recognized in respect of:		
Return on plan assets	(23,147)	(4,201)
Actuarial loss	31,714	1,963
Past service costs	273	273
Transitional obligations	19	15
Net defined benefit pension plan expense	\$ 3,599	\$ 2,904

Total cash payments for employee future benefits for 2008, consisting of cash contributed by the GTAA to its funded pension plans and payments made to the defined contribution plans was \$16.8 million (2007 - \$6.8 million).

The GTAA's plan assets consist of:

Asset Category	Percentage of Plan Assets	
	2008	2007
Equity securities	62%	60%
Fixed income	33%	32%
Cash	5%	8%
Total	100%	100%

The significant actuarial assumptions used in measuring the GTAA's accrued defined benefit pension plan obligations are as follows (weighted-average assumptions as at December 31, 2008):

	2008	2007
Discount rate	7.50%	5.50%
Expected long-term rate of return on plan assets	5.96%	6.02%
Rate of compensation increase	3.50%	4.00%

## 16. Employee Benefits (continued)

### Defined Contribution Pension Plan Expense

The GTAA maintains three defined contribution pension plans providing pension benefits to certain of its employees. The net expense for the defined contribution pension plans is as follows:

(in thousands)	2008	2007
Defined contribution pension plan expense	\$ 2,249	\$ 1,963

The GTAA's contribution to the defined contribution pension plans is a maximum of 6% of the employee's gross earnings. For designated employees of one plan, the GTAA's contribution equals 16% of the employee's gross earnings less amounts already contributed to the plan by the employee and the GTAA.

### Other Employee Future Benefits

Certain employees are provided with paid-up life insurance at the time of retirement, the cost of which is recorded in the period in which the insurance is acquired. The estimated accumulated benefit obligation for this expected payment was \$0.5 million and is included in accounts payable and accrued liabilities on the balance sheet.

## 17. Taxation

The GTAA is exempt from federal and provincial income tax and Ontario capital tax.

The GTAA is exempt from real property tax under the *Assessment Act (Ontario)*. However, the GTAA is required to pay each of the Cities of Toronto and Mississauga an amount as calculated in accordance with regulations under the *Assessment Act (Ontario)* as a payment-in-lieu of real property taxes.

## 18. Related Party Transactions

Directors' fees expense for the year ended December 31, 2008 was \$867,041 (2007 - \$767,250).

## 19. Commitments and Contingent Liabilities

### Ground Lease

The GTAA's commitment in respect of annual ground lease airport rent based on the amendment signed in 2008 (see Note 3, Airport subject to ground lease), including ground rent deferral repayments, is approximately \$142.8 million for the year ending 2009 and has been estimated based on GTAA's current forecast of expected revenues at a

## **19. Commitments and Contingent Liabilities (continued)**

approximately \$131.2 million for the year ending 2010, \$138.3 million for the year ending 2011, \$140.8 million for the year ending 2012 and \$143.8 million for the year ending 2013.

### **Capital Commitments**

In connection with the operation and development of the Airport, the GTAA had capital commitments outstanding at December 31, 2008 of approximately \$159.8 million (2007 - \$262.5 million).

The GTAA would be required to pay a Deficiency Rent (see Note 3, Airport subject to ground lease) equal to any shortfall which may exist between actual eligible capital expenditures and target capital expenditure amounts established in the Ground Lease. Target capital expenditure amounts, subject to adjustments for inflation, were set at approximately \$422.0 million by December 31, 2001 and \$345.0 million by December 31, 2006, both of which the GTAA has met. Target capital expenditure amounts, subject to adjustments for inflation, have also been established for the five-year periods ending December 31, 2011 and 2016 at \$313.0 million and \$835.0 million, respectively, with total target capital expenditures aggregating \$1.92 billion. The GTAA has met this capital expenditure target.

### **Letters of Credit**

A letter of credit for \$2.25 million was outstanding at December 31, 2008 (see Note 13, Credit facility and long-term debt), relating to the GTAA's Clean Energy Supply contract with the Ontario Power Authority. The letter of credit expires April 11, 2009.

### **Environmental**

The GTAA is committed to ensuring that activities undertaken at the Airport are carried out in an environmentally responsible manner, in compliance with applicable environmental laws and regulations, and with sensitivity to community and public concerns.

The GTAA performs environmental assessments as part of its ongoing environmental management program and has achieved ISO 14001 certification.

### **Roadway Infrastructure**

In connection with receiving a deferral for the payment of land transfer tax to the Province of Ontario until 2011 (see Note 13, Credit facility and long-term debt), the GTAA agreed to participate in the development of highway infrastructure and transit improvements related to the Airport. The GTAA has undertaken significant transportation infrastructure work in meeting this requirement.

## **19. Commitments and Contingent Liabilities (continued)**

### **Boeing Lands**

In July 2001, the GTAA and Boeing Canada Operations Ltd. (formerly Boeing Toronto, Ltd.) ("Boeing") signed an agreement, amended in June 2002, under which Boeing agreed to sell to the GTAA 45.73 hectares of land adjoining the Airport property for a total of \$30.0 million. These lands will be transferred by Boeing in stages. The first parcel representing 16.1 hectares of land was conveyed on May 29, 2006 and the remaining lands will be conveyed from time to time over a maximum period of 20 years from that date. While the GTAA retains use of the land, title to the first parcel has been transferred to the federal government as required under the terms of the Ground Lease. Deposits totalling \$4.7 million, which are recorded in work in process, have been made and will be applied to the purchase price of the future parcels.

### **Insurance**

The Government of Canada has issued an Order in Council providing full indemnity to the Canadian aviation industry for any coverage that was lost due to the cancellation of war and terrorism insurance. The Order in Council has been approved for 2008. Official declarations of its status occur every 90 days to account for the potential of change in the insurance industry. As part of the original Order in Council of September 2001, the GTAA was required to purchase a \$50.0 million primary layer of war and terrorist coverage from the commercial markets. This coverage is in place for 2009.

### **Cogeneration Facility**

The GTAA has entered into certain contracts in order to secure the supply and delivery of natural gas necessary for anticipated future operations of the Cogeneration facility. Under these contracts, the GTAA will be required to make payments relating to both the delivery of natural gas based on standard rate agreements and the cost of natural gas as determined by market rates. The delivery contract establishes a maximum volume of natural gas inventory that the GTAA is permitted to maintain, as of the anniversary date. The GTAA has the option to dispose of natural gas in excess of this maximum volume either through consumption or through the sale of natural gas to third parties.

### **Contingent Liabilities**

The GTAA is subject to legal proceedings and claims, from time to time, which arise in the normal course of business. Where appropriate, the GTAA has recorded provisions or reserves while it actively pursues its position. Where it is the opinion of management that the ultimate outcome of these matters will not have a material effect upon the GTAA's financial position, results of operations, or cash flows, no provisions have been recorded.

## **19. Commitments and Contingent Liabilities (continued)**

### **Air France**

Subsequent to the Air France incident on August 2, 2005, the GTAA, together with other parties, is a defendant in ten lawsuits, including a class action lawsuit involving most passengers and their family members. The GTAA's insurers are defending the lawsuits. It is the opinion of management that the GTAA's financial exposure is limited to its insurance deductible.

## **20. Guarantees**

In the normal course of operations, the GTAA provides indemnification agreements to counterparties in a wide variety of transactions such as contracts for goods and services, maintenance agreements, design-build contracts, construction contracts, and information technology agreements. These indemnification agreements require the GTAA to indemnify the counterparties in respect of costs incurred as a result of certain changes in the underlying nature of the contracts (including, without limitation, changes in laws, delays caused by the GTAA, pre-existing environmental conditions) and in respect of costs incurred as a result of certain litigation claims that may result from the transaction (such as, by way of example, patent infringement or personal injury and property damage due to the GTAA's negligence). The terms of the indemnification agreements will vary based on the contract. The nature of the indemnification agreements prevents management from making a reasonable estimate of the maximum potential amount the GTAA may be required to pay to or expend on behalf of such counterparties because such limits are most commonly not set out in the said agreements and the events in question are themselves highly contingent and variable in nature. Management attempts to limit its liability in respect of the indemnifications provided to such counterparties through the purchase of liability and property insurance and the allocation of risk to other contractors.

## **21. Financial Instruments**

Reserve and other funds, other investments, accounts receivable, accounts payable and accrued liabilities and security deposits are reflected in the financial statements at values which approximate fair values because of the short-term nature of these instruments except for ABCP which is fair valued using a valuation technique discussed in Note 6, Reserve and other funds, as no observable market exists.

Fair value represents the amount that would be exchanged in an arm's length transaction between willing parties who are under no compulsion to act and is best evidenced by a quoted market price, if one exists. The GTAA's fair values are management's estimates and are generally determined using market conditions at a specific point in time and may

## 21. Financial Instruments (continued)

not reflect future fair values. The determinations are subjective in nature, involving uncertainties and the exercise of significant judgement.

### Risk Management

In the normal course of business, the GTAA is exposed to a number of financial risks that can affect its operating performance. The GTAA's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the GTAA's financial performance.

The GTAA's central treasury function is responsible for the procurement of the Corporation's capital resources and for the management of financial risk. All treasury operations are conducted within policies and guidelines approved by the Board of Directors and are within the requirements set out in the Trust Indenture dated December 2, 1997. Compliance with these policies is monitored by the regular reporting of treasury activities to the Board.

The GTAA's operating activities result in financial risks that may arise from changes in market risk, credit risk and liquidity risk.

### Market Risk

#### (a) Interest rate risk

The GTAA's exposure to interest rate risk relates to its floating rate bank indebtedness and medium term notes as described in Note 13, Credit facility and long-term debt. It should be noted that the majority of GTAA's debt is fixed rate debt and therefore changes in interest rates do not significantly impact interest payments but may impact the fair value of this debt. An increase of 100 bps in Bankers' Acceptance interest rates applied to the average floating rate bank indebtedness and medium term notes outstanding during 2008 would have increased interest expense by approximately \$6.5 million. The Debt Service Reserve Fund for bank indebtedness is adjusted annually on December 2 based on the prevailing Bankers' Acceptance rate.

In addition to the floating rate debt discussed above, the GTAA also has exposure to floating rate assets through its short-term investments in reserves and other funds (see Note 6, Reserve and other funds). Movements in the reference rates for floating rate debt and assets are highly correlated. Movements in interest rates which have the effect of increasing borrowing costs will also increase interest income from the floating rate assets. To the extent that the amount of floating rate debt is similar to the amount of floating rate assets, the effect of the changes in interest rates on the GTAA would be mitigated.

## 21. Financial Instruments (continued)

### (b) Commodity price risk

The GTAA's exposure to commodity price risk relates to its Clean Energy Supply Contract with the Ontario Power Authority. The impact of a 1% increase in the 2008 average price of electricity holding natural gas prices constant would result in a \$1.6 million decrease in the fair value of the OPA derivative. The impact of a 1% increase in the 2008 average price of natural gas holding the price of electricity constant would result in a \$1.1 million increase in the fair value of the OPA derivative.

### (c) Foreign currency rate risk

The GTAA undertakes certain transactions denominated in foreign currencies, primarily the U.S. dollar. The GTAA's exposure, however, to any foreign currency risk is not significant.

### **Credit Risk**

The GTAA is subject to credit risk through its financial assets. The GTAA performs ongoing credit valuations of these balances and maintains valuation allowances for potential credit loss.

The credit quality of financial assets that are neither past due nor impaired can be assessed by reference to external credit ratings (if available) or to historical information about the customer:

## 21. Financial Instruments (continued)

(in thousands)	2008	2007
<b>Accounts receivable</b>		
Customers with external credit rating:		
AA-	\$ 864	\$ -
A+	910	-
BBB	883	739
BBB-	892	716
B+	-	619
B	7,927	10,565
B-	1,398	1,745
	<b>12,874</b>	<b>14,384</b>
Customers without external credit rating:		
Existing customers with no history of default	32,803	40,210
	<b>\$ 45,677</b>	<b>\$ 54,594</b>
<b>Cash and cash equivalents</b>		
AA-	\$ 63,000	\$ -
A-1+	68,000	98,430
A-1	62,911	59,000
	<b>\$ 193,911</b>	<b>\$ 157,430</b>
<b>Reserve and other funds</b>		
AA-	\$ 120,353	\$ -
A+	68,339	-
A-1+	540,784	475,910
A-1	103,330	315,049
ABCP (see Note 6, Reserve and other funds)	65,290	116,161
	<b>\$ 898,096</b>	<b>\$ 907,120</b>
<b>Other investments</b>		
ABCP (see Note 7, Other investments)	\$ 27,040	\$ 28,802
<b>OPA derivative</b>		
AA-	\$ 41,201	\$ -
A-1	-	39,291
	<b>\$ 41,201</b>	<b>\$ 39,291</b>

None of the financial assets that are fully performing have been renegotiated during the year with the exception of ABCP which are currently being restructured (see Note 6, Reserve and other funds).

## 21. Financial Instruments (continued)

The GTAA derives a substantial portion of its operating revenues from air carriers through landing fees and general terminal charges. There is a concentration of service with two air carriers which represents approximately 57% of these fees and 33% of the account receivable balance at December 31, 2008.

### Liquidity Risk

The GTAA manages liquidity risk by maintaining adequate cash, reserves and available credit facilities. Quarterly cash flow projections are prepared and reviewed by the Audit Committee to ensure a sufficient continuity of funding. To maintain a flexible program, debt maturities are spread over a range of dates thereby ensuring that the Corporation is not exposed to excessive refinancing risk in any one year.

The table below analyses the GTAA's financial liabilities by relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The table has been prepared based on the contractual undiscounted cash flows based on the earliest date on which the GTAA can be required to pay. It includes both principal and interest cash flows.

(in thousands)	December 31, 2008			
	Less than 1 month	1 month to 12 months	1 year to 5 years	Thereafter
Accounts payable and accrued liabilities	\$ 43,269	\$ 41,315	\$ -	\$ -
Province of Ontario	-	-	14,400	9,600
Long-term debt	50,400	643,873	4,294,739	7,956,590
	\$ 93,669	\$ 685,188	\$ 4,309,139	\$ 7,966,190

(in thousands)	December 31, 2007			
	Less than 1 month	1 month to 12 months	1 year to 5 years	Thereafter
Accounts payable and accrued liabilities	\$ 40,928	\$ 36,250	\$ -	\$ -
Province of Ontario	-	-	14,400	9,600
Long-term debt	55,049	1,106,840	4,150,141	7,636,144
	\$ 95,977	\$ 1,143,090	\$ 4,164,541	\$ 7,645,744

Additional disclosure about the GTAA's credit facility, long-term debt, and OPA derivative can be found in Note 13, Credit facility and long-term debt and Note 10, Other assets.

## 22. Capital Risk Management

The GTAA is a non-share corporation and, accordingly, is funded through operating revenues, AIF revenue, reserve funds, the debt capital markets and its syndicated bank credit facility. Aeronautical charges are set each year to cover the projected operating costs, including debt service and reserve requirements, after consideration of the projected air traffic and passenger activity and non-aeronautical revenues. Consistent with its residual approach, funds generated by the GTAA are used to cover costs within its mandate.

As at December 31, 2008, the net deficiency amounted to \$398.9 million (2007 - \$352.9 million). The GTAA has established, within its net assets (deficiency), funds for operational requirements and debt-related obligations. The net assets (deficiency) consist of three components: externally restricted, internally restricted and unrestricted funds.

### Externally Restricted

A portion of the net assets has been allocated for operational purposes pursuant to the Operating and Maintenance Reserve Fund, the Renewal and Replacement Reserve Fund and the Debt Service Fund – Principal (see Note 6, Reserve and other funds) set out in the Trust Indenture (see Note 13, Credit facility and long-term debt).

### Internally Restricted

A portion of the fees that have been collected in revenue has been allocated for capital projects and for debt-related obligations of notional principal and debt service coverage requirements (see Note 6, Reserve and other funds). In conjunction with the airport improvement fee agreement with the airlines, a portion of the fee that has been collected has been allocated to a reserve fund. The internally restricted net assets are held in separate investment accounts by the GTAA and are disbursed in accordance with its policies or commitments for these funds.

### Unrestricted

Unrestricted net assets (deficiency) represents the cumulative revenue under expenses, including amortization, interest expense incurred and required to fund the Debt Service Fund – Interest, and the cumulative unrealized changes in net assets, which remains after externally and internally restricted reserve fund cash commitments described above have been made.

### Capital Markets Platform

As a corporation without share capital, the GTAA's ongoing capital requirements are financed through the issuances of debt. The GTAA developed a financing program referred to as the Capital Markets Platform, capable of accommodating a variety of

## 22. Capital Risk Management (continued)

corporate debt instruments. All indebtedness incurred under the Capital Markets Platform is secured under the Trust Indenture dated December 2, 1997, and supplemented from time to time, which establishes common security and a set of common covenants by the GTAA for the benefit of its lenders. The security comprises an assignment of the revenues of the GTAA, a specific charge on certain funds, reserve funds and accounts, an unregistered first leasehold mortgage of the GTAA's leasehold interest in the Airport and a guarantee and related collateral security of subsidiaries as designated from time to time. The Debt Service Reserve Funds are funded from the net proceeds of each bond or medium term note issuance (see Note 6, Reserve and other funds). The covenants that the GTAA must meet include two specific coverage tests for operating expenses and debt payments. The operating covenant states that the total revenue must at least cover all operating expenses, including interest and financing costs. The debt service covenant states that the net revenues, which may include available credit, must be at least 1.25 times the total interest and financing costs, including notional principal. At December 31, 2008, the GTAA was in compliance with the above covenants and was not in default of the Trust Indenture as defined therein.

## 23. Subsequent Events

### (a) Asset Backed Commercial Paper

On January 12, 2009, the Ontario Superior Court of Justice issued the implementation order for the restructuring of ABCP. The restructuring was implemented effective January 21, 2009 and the GTAA received the following restructured notes under the plan:

- \$61.7 million MAV II Class A1 notes, rated "A" by DBRS with an expected term to maturity of approximately eight years;
- \$59.1 million MAV II Class A-2 notes, rated "A" by DBRS with an expected term to maturity of approximately eight years;
- \$10.7 million MAV II Class B notes, which are unrated and have an expected term to maturity of approximately eight years;
- \$4.1 million MAV II Class C notes, which are unrated and have an expected term to maturity of approximately eight years;
- \$2.1 million Traditional Asset Tracking Notes in one class which are unrated and have an expected term to maturity of approximately five years;
- \$43.1 million Ineligible Asset Tracking Notes in four classes which are unrated and have expected terms to maturity from five to twenty-two years.

The MAV II Class A-1 and A-2 notes and the TA and IA Tracking notes pay interest on a quarterly basis at variable interest rates. It is not expected that the MAV II Class B and C notes will pay current interest, instead interest will accrue and to the extent possible be

## **23. Subsequent Events (continued)**

paid after the Class A-1 and A-2 notes are repaid.

The market for these notes is currently characterized by a low volume of trades and wide bid/ask spreads. Lacking reliable market data to use in determining the fair value of the restructured notes, the GTAA estimated the fair value using a method consistent with the methodology described in Note 6, Reserve and other funds.

As at January 21, 2009, the GTAA estimate of the fair value of the notes was not significantly different from the year-end value. On closing of the restructuring, the GTAA received \$6.2 million representing interest accrued on the ABCP from August 2007 to August 2008, net of restructuring costs and reserves. An additional payment representing accrued interest for the period September 2008 to the restructuring date will be paid at a later date. Due to the high degree of uncertainty regarding payment of interest on the ABCP, the full amount of this payment was not accrued in the financial statements of the GTAA in 2007 or 2008 and, accordingly, a portion of this payment will be reflected in the 2009 financial statements.

### **(b) Repayment of Medium Term Note**

On February 4, 2009, the Series 2004-2 medium term note matured. The \$250.0 million medium term note was repaid using a combination of cash, short-term investments and reserve funds.

## **24. Comparative Figures**

Certain comparative figures have been reclassified to conform with the current period's presentation.