The interest, depreciation, and sinking funds for the year absorbed the sum of 443,546.83

Leaving a balance of net surplus earnings for the year after meeting all charges applicable thereto, of $34,575.87

The whole of the cost of getting and promoting new business amounting to upwards of $60,000.00 has again been met out of the year's income.

During the last quarter of the year a careful appraisal was made by the General Manager of the wearing lifetime and the residual values of the physical plant and equipment and the depreciation appropriation for the year, which is substantially larger than that of last year, has been based upon that appraisal. The amount set aside for depreciation in 1912, though quite sufficient to cover the actual wear and tear of the plant and equipment for that year—the first complete working year it had been in use—was, however, based, pending an appraisal of the wearing lifetime of the different parts of the plant, upon a tentative rate only. It is unnecessary to emphasize the capital importance of establishing and maintaining out of income a fund from which to maintain the physical plant in the highest state of efficiency, and to replace the various parts thereof as they wear out. This is a first principle in sound finance. No departure therefrom is capable of justification.

The Sinking Fund appropriation covers the amount required for the year under the three governing city by-laws, together with interest on past due instalments. The Sinking Fund Suspense Account likewise annexed hereto gives full details of the amount of $94,617.20, which is carried forward as a charge upon the surplus earnings of 1914 and future years. The Corporation of the City of Toronto is under a contract obligation to the debenture holders to maintain sinking funds in accordance with the terms of the governing by-laws. These obligations have been quite properly charged by the Corporation against and assumed by the Hydro-Electric System The total amount thereof at the 31st December, 1913, was $289,211.16. From this total there has been deducted:—

(a) The provision made out of income for the year 1912, representing a full year's instalment and interest thereon on the actual net debt of the System as at the end of that year.

(b) The provision made out of income for the year 1913, representing a full year's instalment as required by the first two by-laws, and a half year's instalment as required by the terms of the third by law and interest thereon.

(c) The surplus earning for the year 1912; and,

(d) The surplus earnings for the year 1913, thereby leaving a net balance as aforesaid of $94,-617.20 to carry forward against future profits.

Had the enterprise been conducted as a commercial corporation, with share capital instead of being charged with debenture capital subject to repayment, the net earnings for the year would have been shown at the amount of $312,164.14, that being the sum of the interest and sinking fund appropriations and the net surplus, or the equivalent of a dividend at the rate of 7½ per cent. upon the average amount of cash capital invested therein.

Additions have been made to the physical system beyond the limits covered by by-laws 5036 and 5918, in respect of—

(a) Certain requirements of the street and park lighting system.

(b) A 13,200 volt commercial power distribution system.

(c) Some special equipment in connection with the civic car lines; and

(d) Certain other increases in general capacity, at a cost of approximately $620,000. To cover this expenditure by-law No. 6674, authorizing the issue of $700,000 of 4½ per cent. **sinking fund debentures,** dated 1st July, 1913, and maturing on the 1st July, 1953, was passed by the Corporation of the City of Toronto on the 13th October, 1913, and duly sanctioned by the Ontario Railway and Municipal Board.

The total expenditure authorized by and the net proceeds of the debentures issued under the three by-laws are as follows:—

By-Law No.	Estimated Cost of System.	Actual Cash Proceeds of Debentures.	P.C. of Face Value.	Discount and Expenses on Debentures.	P.C of Face Value.	Amount of Debenture Issues Authorized.	
5036 (4%)	$2,500,000	$2,240,124 55	81.46%	$509,875 45	18.54%	$2,750,000	100%
5918 (4%)	2,000,000	1,816,774 89	82.58%	383,225 11	17.42%	2,200,000	100%
Total	$4,500,000	$4,056,899 44	81.96%	$893,100 56	18.04%	$4,950,000	100%
6674 (4½%). Est'd. cost..	620,000	....	......	....	......	....	.....
Cash proceeds, till 31-12-13	......	431,464 51	......	....	......	....	.....
Cash proceeds, Jan., 1914..	......	209,870 49	91.62%	....	......	....	.....
Discount till 31-12-13......	......	....	......	39,967 50	......	....	.....
Discount till Jan., 1914 ..	......	....	......	18,697 50	8.38%	....	.....
Debs. issued	......	....	......	....	......	700,000	100%
Grand total	$5,120,000	$4,698,234 44	83.15%	$951,765 56	16.85%	$5,650,000	100%

Of the total estimated expenditure of $5,120,000, authorized by the aforesaid by-laws, the sum of $4,-619,539.20 had been expended up to the 31st December last, leaving a balance of $500,460.80 available for construction work not then finished. It is anticipated that this will suffice to complete the work included in the above estimates. It is to be noted, however, that the net proceeds of the total issues of debentures amount only to the sum of $4,698,234.44, or $421,765.56 short of the estimated cost of complete construction. This deficiency will require to be made available for the use of your Commission as it is required.

It is important that the necessities of the System in respect of working capital be clearly explained. No provision has yet been made for furnishing the enterprise with any capital except that required for purely construction purposes. In addition to the capital funds invested in plant and equipment there will always be a large amount invested in stores on hand, in accounts receivable outstanding, and in sundry other directions. The funds so invested must either be obtained from the general creditors, from the free part of the accumulating depreciation reserves, from the accumulating surplus earnings, or by way of additional capital. Creditors, however, require to be paid and paid promptly if satisfactory business is to be maintained. The depreciation reserves may be employed to some extent as working capital, but it is neither sound nor possible that they be wholly monopolized for that purpose. The policy of carrying on the system at cost for the benefit of consumers will prevent the accumulation of surplus earnings on a large scale. If they should be so accumulated it means the maintenance of profit yielding rates instead of rates based on cost. Therefore, if the funds required for these additional necessary investments are neither contributed by creditors nor by surpluses, they must be provided by way of additional working capital.

The amount required as at 31st December last by way of working capital is as follows:—

Stores investment	$231,511.51
Accounts receivable	351,748.12
Prepaid charges	3,582.31
Sinking fund obligations carried forward..	94,617.20
	$681,459.14
Less depreciation reserves accumulated ..	246,647.77
	$434,811.37

It is not likely that the funds invested in stores on hand and represented by accounts receivable will ever be placed permanently at a lower level than that at which they stood at the 31st December last. On the contrary, it is most probable that, with a continuation of the growth of the System, the amounts invested in stores and outstanding in respect of accounts receivable will reach, from time to time, still higher levels. The amount temporarily required to make good sinking fund obligations will, of course, be recovered from future income, upon which it is a charge. The foregoing figures make it quite clear that, at the present stage of development, working capital over and above the amount provided for construction capital should be furnished to the minimum extent of half a million dollars, but having in view the expansion of the System, and the necessity for keeping a portion of the depreciation reserves always available for the true purposes of the fund, arrangements ought to be made for placing at the disposal of the Commission working capital, to be availed of as required, to the extent of an even million dollars. The amount required could either be raised by the Corporation direct or by the Commissioners on the credit of the Corporation. Special powers would probably be required to cover either method. The better method would be that of authorizing the Commissioners to borrow on the credit of the city, as in that event they would only employ the funds as to the amount and for the periods required, thereby saving unnecessary interest charges. Pending the grant of the necessary working capital, or in the alternative the accumulation of surpluses to the required amount, it is of course obvious that the current debt to the Corporation of the City of Toronto in respect of interest and sinking funds amounting to the sum of $563,337.21 cannot be fully discharged. The importance, therefore, of making early arrangements in this matter is self-evident.

PROGRESS DURING 1913:

Very satisfactory progress has been made during the year 1913, both in respect of the services rendered the public and in respect of the internal administrative and operating efficiency. The following table shows the growth in the services rendered the public:—

Particulars.	At 31st Dec., 1912.	At 31st Dec., 1913.	Increase.
Meters in use	13,858	24,999	11,141—80%
Street lanterns in use	33,824	38,944	5,120—15%
	December, 1912.	December, 1913.	
Peak load H.P.	17,198	22,520	5,322—31%

The growth of income and the improvement in administrative and operating efficiency are clearly set forth in the comparative statements annexed to the accounts herewith. The principal features thereof may be summarized as follows:—

The total income has increased from $726,763.55 in 1912 to $1,159,339.71 in 1913, a gain of $432,576.16, or nearly 60 per cent. The commercial income has grown from $338,262.64 in 1912 to $684,622.36 in 1913, a gain of $346,360.28, or 102½ per cent. The net surplus, after providing for all fixed charges, has grown from $13,555.41 in 1912 to $34,575.87 in 1913. a gain of $21,020.46, or 155 per cent. That is to say, that the total income has increased by 60 per cent.; the commercial income has more than doubled itself; and the net surplus earnings, after providing for all fixed charges applicable to the year's operations, are over two and one-half times what they were in 1912. The cost of current has been reduced by 4 2-3 per cent., and the expenses of operation, maintenance and management have been reduced by nearly 5½ per cent. The decrease in the cost of current is due in part to the reduction of price by the Provincial Commission, and in part to the improved engineering management of the present general manager, the load factor of 1912 being 59.5 per cent., while that of 1913 was 70.4 per cent. That is to say, that the better distribution of load, and the better keeping down of the peak load during 1913, led to an actual consumption of 70.4 k.w.h. units out of each 100 units bought and paid for, as against a consumption of only 59.2 k.w.h. units in 1912 out of each 100 units then bought and paid for. The reduction of nearly 5½ per cent. in the ratio of operating expenses is due to the growth of business and to the efficient management of Mr. Couzens. These gains are the more pleasing by reason of the costly circumstances mentioned in the first paragraph hereof.

There has been an increase in the ratio of interest to income of 4.39%, and in the ratio of depreciation to income of 4.87%. The interest increase is due to the heavy additional burden laid upon the enterprise by being charged with the loss of $933,068.06 arising out of the sale of the debentures, for which, of course, no value has been received. The increase in the depreciation ratio is due to the heavier necessary provision made therefor, under the appraisal of the wearing lifetime of the plant referred to above.

ENLARGEMENT OF THE SYSTEM:

The growth of the city, to which attention was drawn last year, continues in undiminished degree. There are now 520 miles of streets lighted by the Hydro-Electric System, as against 280 miles at the time of the inception of the enterprise. Enlargements of the system to overtake the obligations arising out of the city's growth will be necessary from time to time. The interruptions of service during the past year on the lines of the Provincial Hydro-Electric Commission through insulator troubles have established the necessity of providing an auxiliary steam reserve plant that will take care of the load during temporary breakdowns. At a joint conference held by the Provincial Commission and your Commissioners during the year, a formal decision was taken to instal, as soon as possible, the necessary Steam Reserve Plant. The estimated capital cost thereof is approximately $1,000,000. The carrying and the operating charges thereof will add substantially to the annual charges of the system, but this extra cost must be regarded as a relatively cheap insurance against the heavy penalties that otherwise would have to be borne by the power and light consumers on account of service interruptions from time to time, proceeding from uncontrollable causes.

REDUCTION OF RATES:

In the last Annual Report your Commissioners expressed the opinion that with a continuation of satis factory surpluses a reduction of rates might possibly be effected during the year 1914. During the interval, however, three conditions have arisen not then contemplated, which combine to defer for the time being any possible reduction of rates. In the first place, the interruptions of service on the Provincial Hydro lines, which have since occurred, have, as already stated, established the necessity of providing a Steam Reserve Plant, the heavy annual charges of which will constitute an additional burden on the System, not then contemplated or allowed for. In the second place, it was not anticipated at that time that the enterprise would be loaded with the heavy additional burden since laid upon it by reason of the low prices at which the Corporation of the City of Toronto found it necessary to sell the debentures authorized by the first two by-laws. The discount and expenses of these two debenture issues amount, as set forth in the second paragraph hereof, to the sum of $893,100.56, or 18.04% of the face value of the issues, while the total flotation cost of the three issues amounts to $951,765.56, or 16.85% of the face value thereof—that is a little over 20% of the amount of the net proceeds. That is to say, that each hundred dollars of cash invested in plant has cost by reason of these heavy expenses a little over $120.00. The additional annual burden laid thereby upon the enterprise until the maturity of the deben-