

Obligatory Reserve Funds (Deferred Revenues), Reserves, and Council-directed Reserve Funds Report – September 30, 2020

Date: November 2, 2020
To: Budget Committee
From: Chief Financial Officer and Treasurer
Wards: All

SUMMARY

This report summarizes the changes impacting the City of Toronto (the City)'s obligatory reserve funds (deferred revenues), reserves, and Council-directed reserve funds as at September 30, 2020.

The City's deferred revenues (obligatory reserve funds), reserves, and Council-directed reserve funds are subject to annual changes based on funding contributions, transfers, and drawdowns, which are authorized by legislation, third-party agreements, and Council's approvals. The tables and appendices reflect information by major category.

As at September 30, 2020, the City recognized \$7,239.9 million of deferred revenues (obligatory reserve funds), reserves, and Council-directed reserve funds, which consist of the following balances:

- Committed funds for legislated, contractually bound or Council-directed activities (\$6,166.7 million);
- Committed funds to offset capital costs and pressures on rate-based activities (\$751.3 million); and
- Uncommitted and available funds for the City to respond to various unanticipated costs and to stabilize various funding sources, including the tax base (\$321.9 million).

The reported balances include Council approved reserve and reserve fund loans that were granted to various agencies, City programs, and external parties, which must be repaid to the respective deferred revenues (obligatory reserve funds), reserves, and Council-directed reserve funds.

RECOMMENDATIONS

The Chief Financial Officer and Treasurer recommends that:

1. Budget Committee receive this report for information.

FINANCIAL IMPACT

There are no financial implications contained in this report.

DECISION HISTORY

As per Chapter 227 of the Municipal Code, the Chief Financial Officer and Treasurer will report inflows and outflows of the City's deferred revenues (obligatory reserve funds), reserves, and reserve funds on a quarterly basis, to the Budget Committee. To view prior period reports online, please see the links below:

Obligatory Reserve Funds (Deferred Revenues), Reserves, and Council-directed Reserve Funds Report – June 30, 2020

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2020.EX16.13>

Reserves, Council Directed and Obligatory Reserve Fund (Deferred Revenue) Balances Report – September 30, 2019

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2019.EX11.18>

COMMENTS

Background

Reserves and reserve funds represent an allocation of the City's funds, which have accumulated over time and may be used to replace capital assets, provide a measure of financial flexibility to react to budget funding shortfalls, and to address the financial impacts of significant unexpected issues in a timely manner.

These funds are managed to achieve an optimal rate of return on a risk-adjusted basis in accordance with the Council –approved Investment Policy. Shorter term funds are managed internally to meet cashflow needs, while funds not immediately required are guided by the Toronto Investment Board who has contracted external investment managers to handle longer term commitments.

Deferred revenues (obligatory reserve funds) represent funds received by the City that are recognized as earned revenue only after the delivery of required performance obligations. Deferred revenues represent liabilities that the City must settle in the future.

A properly balanced approach to the planning and use of reserves and reserve funds is considered good financial management and is a key component of the City's strong credit rating. The City has a formal policy to align with best practices, support the stewardship and oversight of reserves and reserve funds, and demonstrate accountability.

A summary of the major financial balances that are referenced throughout this report, is as follows:

- Deferred revenue (obligatory reserve funds): advance payment for goods and/or services that the City has not yet provided to a government, government organization, third-party entity, or individual. Deferred revenues are only taken into income with the execution of activities or stipulations specified in legislation, contract, or agreement. These balances earn interest, and are reported as a liability in the City's consolidated financial statements.
- Reserve: an allocation of accumulated net revenue, which can be set aside for a specific use and does not reflect earned interest. Reserves are disclosed in the City's accumulated surplus in the City's consolidated financial statements.
- Council-directed reserve fund: funds earning interest income that have been set aside in response to a by-law. Similar to reserves, Council-directed reserve funds are a component of the City's accumulated surplus, which is disclosed in the consolidated financial statements.

Deferred revenues (obligatory reserve funds), reserves, and Council-directed reserve funds are impacted by the following types of transactions, which occur throughout the year:

- Budgeted transfers: fund inflows and outflows made in accordance with Council's approvals during the regular budgeting cycle, or through ad hoc requests.
- Deferred revenue changes: receipt of cash payments made prior to the City's provision of a good and/or service, as well as reduction of the overall balance to account for amounts earned as revenue subsequent to the satisfaction of a legislative requirement or terms and conditions of a third-party contract or agreement.
- Loans from deferred revenues (obligatory reserve funds), reserves and reserve funds to finance various operating and capital programs (e.g. Residential Energy Retrofit Pilot) using interest-free or low interest arrangements. The loans are managed through formalized agreements and are repayable back to the deferred revenue (obligatory reserve fund), reserve, or reserve fund within five to 50 years.
- Interest income allocations: earnings allocated to deferred revenues (obligatory reserve funds) and Council-directed reserve funds on an annual basis based on the interest forecasted to be earned from three-month Treasury Bills at the time of the preparation of the annual operating budget.

Deferred revenues (obligatory reserve funds), reserves and reserve funds balance as at September 30, 2020

As at September 30, 2020, the City recognized a deferred revenues (obligatory reserve funds), reserves, and reserve funds balance of \$7,239.9 million (2019: \$6,059.0 million); this balance includes loans receivables of \$69.1 million. The City's deferred revenues (obligatory reserve funds), reserves, and reserve funds balance increased by \$1,180.9 million or 19.49%, which resulted mainly from the following activities:

- Transfer of \$684.7 million from Water and Wastewater programs to the Water and Wastewater Capital Reserve Fund for capital financing;
- Receipt of \$277.4 million of development charges, park levies and Section 37 funds;
- Contribution of \$68.6 million to the City Building Reserve Fund from Non-program;
- Contributions of \$59.4 million to the Vehicle & Equipment Replacement Reserve from operating divisions during the first nine months of the year.

The City will allocate interest income to the deferred revenue (obligatory reserve funds) and Council-directed reserve fund balances at year-end. The 2020 rate, which is applicable for current year's allocations, decreased slightly to 1.57% from 1.65% in 2019.

The following table summarizes the City's total deferred revenue (obligatory reserve funds), reserve, and reserve fund balance, which includes loans receivable balances, as at September 30, 2020, with a comparison to December 31, 2019. A separate report for the City's deferred revenue (obligatory reserve funds), reserves and reserve funds as at December 31, 2019 has not been presented to City Council. However, all of fiscal 2019's balances were included in and examined as part of the scope of the City's external audit to support the preparation of the 2019 consolidated financial statements. The audited balances are included in this report. In addition, it should be noted that the presentation of the December 31, 2019 balances in the below table and appendices has been modified from previous reports to align with the presentation in the City's financial statements.

Table 1: Overview of deferred revenues (obligatory reserve funds), reserves, reserve funds, and loans receivables (\$ millions)

	Sep. 30, 2020	Dec. 31, 2019
Deferred revenues (obligatory reserve funds):		
<i>Restricted by Provincial legislation</i>		
Development charges	1,416.5	1,223.3
Parkland acq. / new development	651.0	645.0
Planning Act	374.7	333.0
Provincial Gas Tax revenues for Public Transit ¹	0.0	21.5
Building Code Act service improvement	121.8	122.5
	<u>2,564.0</u>	<u>2,345.3</u>
<i>Restricted by agreements with third parties</i>		
Community services	68.3	68.2
Third party agreements	20.0	20.7
Public Transit funds	174.9	157.1
State of good repair	10.6	10.3
Parking Authority	1.5	1.4
Water / wastewater	1,896.1	1,204.8
	<u>2,171.4</u>	<u>1,462.5</u>
Total deferred revenues (obligatory reserve funds) in the City's consolidated financial statements:	4,735.4	3,807.8
Reserves:		
Corporate	743.6	654.1
Stabilization	223.3	203.1
Water / wastewater	104.5	99.8
Donations	1.8	1.8
	<u>1,073.2</u>	<u>958.8</u>
Council-directed reserve funds:		
Employee benefits	290.8	295.5
Corporate	678.9	573.2
Community initiatives	177.5	177.3
State of good repair	284.1	246.4
	<u>1,431.3</u>	<u>1,292.4</u>
Total reserves and Council-directed reserve funds – accumulated surplus in the City's consolidated financial statements	2,504.5	2,251.2
Total deferred revenues (obligatory reserve funds), reserves, and Council-directed reserve funds	<u>7,239.9</u>	<u>6,059.0</u>

1: The City received \$136.2 million and \$45.4 million in provincial gas tax funding on June 25, 2020 and September 8, 2020, respectively. The City will present the allocation of these installment payments to the provincial gas tax reserve fund for the 2020 year-end Obligatory Reserve Funds (Deferred Revenues), Reserves, and Council-directed Reserve Funds Report, along with any further funding received, if applicable.

Please refer to Appendices A1, B1, and C1 for details supporting the above reserves and Council-directed reserve funds, as well as Appendices A2, B2, and C2 for details supporting the loans receivables.

The following table summarizes the City's loans receivable as at September 30, 2020, with December 31, 2019 comparatives.

Table 2: Overview of loans receivables (\$ millions)

	Sep. 30, 2020	Dec. 31, 2019
Deferred revenues:		
<i>Restricted by Provincial legislation</i>		
Development charges ¹	10.3	10.6
	10.3	10.6
<i>Restricted by agreements with third parties</i>		
Community services	8.2	8.2
	8.2	8.2
Total deferred revenues loans	18.5	18.8
Reserves:		
Stabilization	11.6	11.6
	11.6	11.6
Council-directed reserve funds:		
Corporate	17.3	19.3
Community initiatives	21.7	22.2
	39.0	41.5
Total reserves and Council-directed reserve funds loans	50.6	53.1
Total deferred revenues (obligatory reserve fund), reserve, and Council-directed reserve fund loans	69.1	71.9

1: These balances are associated with loans that the City provided to external parties using the development charges reserve fund. Please refer to Appendix A2 for a list of external parties that have received a loan.

Please refer to Appendices A2, B2, and C2 for details supporting the loans receivables.

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SIGNATURE

Heather Taylor
Chief Financial Officer and Treasurer

ATTACHMENTS

- Appendix A1: Deferred Revenues (Obligatory Reserve Funds) as of September 30, 2020
- Appendix B1: Reserves as of September 30, 2020
- Appendix C1: Council-Directed Reserve Funds as of September 30, 2020
- Appendix A2: Loan Receivable Balances: Deferred Revenues (Obligatory Reserve Funds) as of September 30, 2020
- Appendix B2: Loan Receivable Balances: Reserves as of September 30, 2020
- Appendix C2: Loan Receivable Balances: Council-Directed Reserve Funds as of September 30, 2020