



REPORT FOR ACTION

Additional City of Toronto Reporting Requirement as a Result of Ontario Regulation 286/09, Budget Matters - Expenses

Date: January 30, 2019
To: Budget Committee
From: Chief Financial Officer and Treasurer
Wards: All

SUMMARY

Ontario Regulation 286/09 "Budget Matters - Expenses" (Regulation) allows the City of Toronto (City) to exclude amortization expense, post-employment benefit expenses and solid waste landfill closure and post-closure expenses when preparing its annual budget. The Regulation requires that the City prepare a report which includes at a minimum, an estimate of the change in accumulated surplus resulting from the exclusion of the noted expenses from the budget and an analysis of the impact of the exclusion on future capital asset funding requirements. The Regulation requires that this report be adopted by City Council (Council) prior to the adoption of its annual budget.

To meet the requirements of the Regulation, this report discusses the impact of excluding amortization expense, post-employment benefit expenses and solid waste landfill closure and post-closure expenses from the City's budget, along with the impact of the differences between how the City treats the purchase of tangible capital assets, debt principal repayments, Government Business Enterprise (GBE) earnings, and expenses arising from contaminated site liabilities for budgeting and financial reporting purposes. The treatment of the expenses beyond those identified in the Regulation is included to reflect the complete impact on estimated accumulated surplus for 2019.

RECOMMENDATIONS

The Chief Financial Officer and Treasurer recommends that:

1. City Council receive this report for information.

FINANCIAL IMPACT

There are no financial implications as a result of this report.

S. 228 of the City of Toronto Act requires that the City prepare an annual balance budget, which does not create a budgeted surplus or deficit. The City's 2019 operating and capital budgets include all entities funded through tax and rate based programs, including agencies and corporations.

For financial reporting purposes, a surplus or deficit amount is created when revenues and expenses are accounted for using PSAB standards. The resulting surplus or deficit increases or decreases the City's accumulated surplus. The estimated 2019 accumulated surplus reported in the City's financial statements, resulting from the consolidation of 123 entities and including the financial results of operating and capital activities, Water and Solid Waste and all agencies and corporations, is estimated to increase by \$2.223B to an estimated \$27.335B. This final amount is comprised mostly of the City's investment in tangible capital assets.

DECISION HISTORY

As required by the Regulation, this report has been provided to Budget Committee annually since 2010.

To view the last two reports on-line, please follow the hyperlinks below:

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2017.BU30.2>
<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2018.BU41.2>

COMMENTS

The City's 2019 operating and capital budgets are prepared on a modified cash basis. The City budgets for the cash revenues it expects to receive and the cash expenses it expects to pay. However, the City also budgets for limited accruals which represent amounts expected or incurred in the year of the budget, but not actually received or paid until after year end. As a result, the City's operating and capital budgets include cash requirements for capital asset expenditures, debt issuance and repayment and amounts paid in the current year for post-employment benefits and landfill closure and post-closure upkeep.

On the other hand, since 2009, the City's financial statements are prepared in accordance with PSAB standards, which require that governments apply full accrual accounting for all assets and liabilities. PSAB is the standard setter for financial statement reporting for all levels of government in Canada. Following PSAB standards, the assets and liabilities of a government entity are recorded based on expected

receipts and obligations not limited to the current year. The financial statements recognize revenues and expenses based on what was actually paid during the year, but also reflect benefits and obligations that will result in cash receipts or payments into the future. Assets and liabilities are recorded on the City's Statement of Financial Position, which reflects how well off the City is as a result of past investments and future obligations. As a result, capital expenditures that are City assets are capitalized, with the asset value expensed over the life of the asset as amortization. In addition, debt issuance is recorded as a liability that requires future payment. Finally, post-employment benefits and other obligations are recorded as obligations using the present value of the future cost.

The preparation of government financial statements now follow the same accounting standards, increasing transparency and comparability, and recognizing not only how well the government entity did against their plan (the modified cash budget) but whether the government entity was better or worse off because of that plan.

The table below outlines the difference between how the City treats the expenses identified in the Regulation, along with other PSAB reporting changes, for budgeting and financial statement reporting. This information will assist in understanding the impact that the expenses have on the accumulated surplus balance.

Item	Budget Treatment	Financial Reporting Treatment
Capital asset expenditures	Budget annual cash required to purchase or build	Expenditures that qualify as capital assets are capitalized on the Balance Sheet
Amortization	Not budgeted as allowed by the Regulation	Expensed based on the service life of the asset that is capitalized
Debt issuance and repayment	Budget cash from debt issuance as a revenue and budget for repayment as an expense	Issuance and repayment is an exchange of assets and only impacts the Balance Sheet
GBE earnings	Budget expected dividend distribution as a revenue	Record equity in excess of dividend distribution as a revenue
Post-employment benefit expenses	Not budgeted as allowed by the Regulation	Expense the amount to achieve the liability required
Landfill closure and post closure expenses	Not budgeted as allowed by the Regulation	Expense the amount to achieve the liability required

Item	Budget Treatment	Financial Reporting Treatment
Contaminated Sites	Treated the same as Landfill closure and post closure expenses	Expense the amount to achieve the liability required

Change in Accumulated Surplus from Excluded and Other Items

Accumulated surplus is a term used in government financial reporting which mirrors retained earnings in the private sector. The largest component of the City's accumulated surplus is related to its investment in tangible capital assets.

The table below estimates the impact of the change in accumulated surplus for the 2019 fiscal year as a result of the Regulation expenditures excluded from the City's cash budget and other PSAB reporting requirements.

	\$000's	\$000's
Est. accumulated surplus, consolidated Dec 31, 2018		25,111,630
Impact of tangible capital assets:		
Estimated capital asset expenditures	3,017,000	
Amortization	(1,136,000)	
Debt principal repayments	403,000	2,284,000
Impact of government business enterprises:		
Est. Earnings from Government Business Enterprises	60,200	60,200
Impact of post-employment benefits:		
Estimated increase in employee benefits liability	(125,000)	(125,000)
Impact of landfill active and post-closure:		
Estimated decrease in landfill active and post-closure costs	4,500	4,500
Impact of contaminated sites:		
Estimated increase in contaminated sites costs	(700)	(700)
Estimated Surplus for Accounting Purposes		2,223,000
Est. accumulated surplus, consolidated Dec 31, 2019		27,334,630

The December 31, 2018 accumulated surplus balance is an estimate at this time as the City continues its efforts to finalize entries, which include the payment of invoices and accruals for amounts yet to be received or required for reporting purposes.

Given the City's 2019 budget is prepared on a balanced basis, the budget itself is estimated to not impact the actual accumulated surplus. However, the increases and decreases are the result of the differences between cash budgeting and financial reporting:

The estimated capital asset expenditures and debt repayments represent cash budget expenses, however, are not considered expenses for financial reporting purposes therefore they are added to the accumulated surplus. Amortization is not included in the

budget, but is a financial reporting expense therefore must be deducted from the accumulated surplus. The City's continued investment in capital assets contributes an estimated \$2.284B to the 2019 estimated accumulated surplus.

The excess earnings from GBE's (representing the full equity in the GBE less the dividend return) are not included in the City's 2019 budget estimate therefore will increase the City's accumulated surplus.

The changes in post-employment benefit expenses, landfill closure and post-closure costs and contaminated sites represent reporting-specific expenses, which are not cash items and therefore, not budgeted by the City. These amounts will adjust the accumulated surplus balance depending on the increase or decrease in the liability.

The estimated 2019 surplus arising from the expenses excluded by the Regulation and other financial reporting entries is \$2.223B, which increases the City's accumulated surplus for financial statement reporting purposes to an estimated \$27.335B at December 31, 2019.

Staff are not recommending that Council move to a full accrual basis of budgeting at this time, as the existing process for capital, through the City's Ten Year Capital Program, and operating budgets, provides for a transparent process to commit funds for current and future years. Budget reports, the Annual Financial Report, reports of progress against the City's Long-Term Fiscal Plan, and additional reports on various initiatives, provide detailed information about the City's financial performance which assists users of the information in understanding the financial position of the City.

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SIGNATURE

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