

Deferred Revenue Report at September 30, 2022 and Administrative Amendments to Obligatory Reserve Fund

Date: March 7, 2023
To: Executive Committee
From: Chief Financial Officer and Treasurer
Wards: All

SUMMARY

The City of Toronto (City) receives monies from external parties and are obligated to set aside for specific purposes outlined in Provincial legislation, third party agreements, or for goods and services that will be provided in the future. These monies create obligations for the City that must be settled at a future date, such as the collection of development charges when building permits are issued that will pay for the cost of infrastructure required to provide municipal services that support the growth of the new development. When these monies are received, they are recognized on the City's Statement of Financial Position as a liability labelled deferred revenue. The deferred revenue amounts are recognized as earned revenue only when the committed investment is completed in the Statement of Operations and Accumulated Surplus. This report provides an update of deferred revenue balances and earned revenue for the first nine months of 2022, and deferred revenues balances at September 30, 2022.

As at September 30, 2022, the City recognized \$6,365.3 million in deferred revenues, increased by \$1,553.7 million in monies received and reduced by \$91.7 million in earned revenues. This balance represents accumulated deferred revenue balances, which is a reflection of obligated investments not yet completed to support growth, or goods and/or service commitments that the City must deliver to third parties, not yet earned and recognized as revenue. Deferred revenues are fully committed based on contractual obligations to support growth-related infrastructure investments in the community, or other service or operational obligations.

RECOMMENDATIONS

The Chief Financial Officer and Treasurer recommends that:

1. City Council establish a new obligatory reserve fund called the "Development Charges Reserve Fund – Transit (EELRT)" in Appendix C, Schedule 11 of Toronto Municipal Code Chapter 227, Reserves and Reserve Funds, for the purpose of providing funding for the Eglinton East Light Rail Transit capital project, with criteria set out in Appendix B to this report, and transfer funds from Development Charges Reserve Fund – Transit (Balance) (XR2109), in an amount equivalent to the balance in the former Development Charges Reserve Fund – Transit (Scarborough Subway Extension) (XR2125) that was closed earlier this year, to the new Development Charges Reserve Fund –Transit (EELRT).

FINANCIAL IMPACT

Deferred revenue is recognized as a liability in the Statement of Financial Position that the City must settle, either through investment or the delivery of goods or services, and earned revenue when the committed investment is completed or intended purpose related to the monies has been executed in the Statement of Operations and Accumulated Surplus. As an example, development charges are recorded as deferred revenues when the cash is first received and earned revenue as the growth related infrastructure investments are made. The full amount of the development charge is recognized as earned revenue when the full investment has been completed and is in service.

For budget purposes, deferred revenue is budgeted as earned revenue based on budgeted expenditures in a fiscal year. However, since actual expenditures will vary from planned expenditures, the actual amount of deferred revenue recognized as earned revenue will align with actual expenditures. As a result, contributions to the deferred revenue balance and earned revenues that reduce the deferred revenue balance can differ based on planned versus actual activity.

Deferred revenue funds received in the future and earned revenues from Development Charges may be impacted by provincial legislation, including Bill 23, the More Homes Built Faster Act as early as 2023

DECISION HISTORY

As per Chapter 227 of the Municipal Code, the Chief Financial Officer and Treasurer is required to report inflows and outflows of the City's obligatory reserve funds on a quarterly basis, as well as provide updates to this Chapter of the Municipal Code for required administrative changes. To meet this requirement, this report focuses on the

contribution and earned revenue for Deferred Revenues currently considered obligatory reserve funds.

To view the most recent reports online, please see the links below:

Obligatory Reserve Funds (Deferred Revenues) and Reserves and Discretionary Reserve Funds as at December 31, 2021:

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2022.EX34.18>

Obligatory Reserve Funds (Deferred Revenues) and Reserves and Discretionary Reserve Funds as at September 30, 2021. This report includes prior year administrative changes to Chapter 227 – Administration of Reserves and Reserve Funds:

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2021.EX28.9>

COMMENTS

Overview of Deferred Revenues

Deferred revenues are created when payments are received from third parties that obligate the City to make an investment or settle an obligation in the future. Cash received from these third parties is deposited in the City's bank accounts and a deferred revenue balance is established in the City's financial records as a liability called "Deferred Revenue" until the obligation is satisfied or as required investments are made.

The City's deferred revenues are accumulated from various advance payments, including amounts received from legislated development payments for growth-related infrastructure, government grants that restrict use of funds for specific programs like transit or housing, or third party agreements that outline how funds are expected to support future investments or the cost of operations. Advance payments can also be received from customers who use City services, such as advance payment for rent of City event spaces or City facilities.

Although cash is provided in advance, the deferred revenues are not reserves; the amounts are liabilities that obligate the City to complete an action committed to a third party and for which the monies were received. Deferred revenues are considered liabilities because the amounts must be returned to the third party, if the good, service or investment is not delivered as planned. Deferred Revenue liabilities are recognized on the City's Statement of Financial Position.

When these payments are received, they are considered contributions to the deferred revenue balance. When the good, service or investment for which the funds were intended is delivered, they are recognized as earned revenue in the City's Statement of Operations. It is only when the conditions for use of the funds are met, that the deferred revenue is recognized as earned revenue in the City's financial results.

The timing of earned revenue from deferred revenue balances depends on the type and complexity of performance obligations or stipulations in third party agreements that need to be met. As an example, development charges governed by Provincial legislation make up a significant portion of the City's deferred revenue balance. The amounts paid by developers are recorded as deferred revenue contributions when building permits are issued, but recognition of these amounts into the City's earned revenues is tied to capital infrastructure planning and execution activities that transcend a number of years. Similarly, deferred revenue contributions from third party agreements may require that the City execute on obligations over a number of fiscal years; earned revenue would be recognized as the expenditures incurred to execute on those obligations are also recognized.

Certain agreements, contracts or legislation require that interest be allocated to certain deferred revenue contributions. These interest allocations are recorded as contributions to the individual balances in the fourth quarter of the fiscal year.

Deferred Revenue balances as at September 30, 2022

As at September 30, 2022, the City recorded deferred revenue liabilities in the amount of \$6,365.3 million, an increase of \$1,462.1 million from the December 31, 2021 balance of \$4,903.2 million. Major deferred revenue contributions come from:

- Contributions of \$709.1 million in development and planning act contributions from developers to be earned revenue when critical growth-related capital project costs are incurred;
- Contributions of \$736.7 million from Water and Wastewater rates to be used for the specific provision of water and wastewater services and capital infrastructure; and
- Contributions of \$46.3 million from the Provincial Gas Tax government grant to be used for transit capital infrastructure

During the first nine months of 2022, \$91.6 million was recognized as earned revenue following the completion of performance obligations or activities stipulated in legislation or third party agreements.

Table 1 below summarizes the City's deferred revenues as at September 30, 2022, with comparatives at December 31, 2021.

Table 1: Deferred revenues at September 30, 2022 with December 31, 2021 comparatives (\$ millions)

(\$ millions)	Sep. 30, 2022	Dec. 31, 2021
Deferred revenues:		
Restricted by Provincial legislation		
Development charges	2,813.7	2,263.1
Parkland acquisition/new development	775.8	743.5
Planning Act	482.8	402.7
Provincial Gas Tax revenues for Public Transit	0.0	0.2
Building Code Act service improvement	226.2	183.6
	4,298.5	3,593.1
Restricted by agreements with third parties		
Community services	66.7	66.7
Third party agreements	14.3	15.4
Toronto Transit Commission	103.1	82.2
State of good repair	9.9	9.7
Parking Authority	1.6	1.5
Water / wastewater	1,871.2	1,134.6
	2,066.8	1,310.1
Deferred Revenues as at September 30, 2022:	6,365.3	4,903.2

Appendix A provides details of deferred revenue contributions and earned revenues by deferred revenue type that make up the total deferred revenue balance at September 30, 2022.

Administrative Amendments to update Chapter 227

Administrative amendments are made to individual deferred revenue balances in Chapter 227 of the Municipal Code annually as part of this report. At its meeting on February 18, 2021, Council adopted EX21.2 2021 Capital and Operating Budgets, redirecting \$1,238.0 million in funding for the Scarborough Subway Extension to the Eglinton East LRT, which included deferred revenue contributions from development charges received for transit infrastructure. The following is a link to Council direction:

<http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2021.EX21.2>

It is recommended that a new reserve fund called "Development Charges Reserve Fund – Transit (EELRT)" be established to provide funding for the Eglinton East LRT capital project. The criteria for this account are set out in Appendix B.

Through the 2023 budget process, Council approved a transfer of the balance in Development Charges Reserve Fund – Transit (Scarborough Subway Extension) (XR2125) to the Development Charges Reserve Fund - Transit (XR2109). Council is requested to transfer an amount equivalent to this balance from XR2109 to the above noted new reserve fund.

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SIGNATURE

Heather Taylor
Chief Financial Officer and Treasurer

ATTACHMENTS

Appendix A: Deferred Revenues as at September 30, 2022

Appendix B: Development Charges Reserve Fund – Transit (EELRT)