

Deferred Revenue Report at September 30, 2023

Date: November 20, 2023
To: Executive Committee
From: Chief Financial Officer and Treasurer
Wards: All

SUMMARY

The City of Toronto (City) receives monies from external parties and is obligated to set these monies aside for specific purposes outlined in Provincial legislation or third party agreements. These monies may also be set aside for goods and services that will be provided in the future. In both instances, the receipt of these monies creates obligations for the City that must be settled at a future date. An example of such an obligation is the collection of development charges when building permits are issued. These development charges will contribute to the cost of growth-related infrastructure required to provide municipal services that support new development. When these monies are received, they are recognized on the City's Statement of Financial Position as a liability called Deferred Revenue. The deferred revenue amounts are recognized as earned revenue only when the committed investment is completed, and expenditures are recognized as tangible capital assets in the Statement of Financial Position or as operating expenses in the Statement of Operations and Accumulated Surplus. This report provides an update of deferred revenue balances at September 30, 2023, and earned revenue for the period ended September 30, 2023, which is included in the City's Statement of Operations and Accumulated Surplus.

As at September 30, 2023, the City recognized \$7,402.8 million in deferred revenues, increased by \$1,910.5 million in monies received and reduced by \$131.6 million in earned revenues as compared to the December 31, 2022 balance of \$5,623.9 million. This balance represents accumulated deferred revenue balances, which reflect 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 performance obligations. In particular, the City estimates that \$22.7 billion of deferred revenues have been committed over the 2023-2032 period – this indicates that the City's commitments are 3.1 times greater than the amount of deferred revenues recognized as at September 30, 2023.

Future deferred revenue funds received and recognized earned revenues from Development Charges may be impacted by provincial legislation, including Bill 23, the

More Homes Built Faster Act. For instance, Bill 23 is currently estimated to result in a \$2.3 billion revenue loss to the City's growth funding tools over a 10-year period (i.e., 2022-2031), including development charges (\$2.0 billion) and parkland dedication (\$0.3 billion). The complete financial impact to the City remains uncertain. While the Province has committed to making the City whole, this is pending the completion of a provincial audit. The results of the provincial have not yet been shared with the City.

RECOMMENDATIONS

The Chief Financial Officer and Treasurer recommends that:

1. Executive Committee receive the Deferred Revenue Report at September 30, 2023 for information.

FINANCIAL IMPACT

There are no financial implications arising from the adoption of the recommendation in this report.

Deferred revenue, as reflected in the Statement of Financial Position, is recognized as a liability for which the City must fulfill a future obligation, either through investment or the delivery of goods or services, and earned revenue, on the Statement of Operations and Accumulated Surplus, when the committed investment is completed or intended purpose related to the monies has been executed. 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.

As at September 30, 2023, the City recognized \$7,402.8 million in deferred revenues, increased by \$1,910.5 million in monies received predominantly from water and waste water rate revenue and development and planning act contributions; and was reduced by \$131.6 million in earned revenues as compared to the December 31, 2022 balance of \$5,623.9 million.

Future deferred revenue funds received and recognized earned revenues from Development Charges may be impacted by provincial legislation, including Bill 23, the More Homes Built Faster Act.

The Chief Financial Officer and Treasurer has reviewed this report and agrees with the financial impact information.

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 contributions to, and earned revenues for Deferred Revenues currently considered obligatory reserve funds.

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

Deferred Revenue Report at June 30, 2023:
[Agenda Item History - 2023.EX8.4 \(toronto.ca\)](#)

Deferred Revenue Report at December 31, 2022:
[Agenda Item History - 2023.EX6.7 \(toronto.ca\)](#)

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 as a liability in the City's financial records 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 operating programs. 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 revenue balances 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 and Accumulated Surplus. 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 several 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 in the future 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 were recorded as contributions to the individual balances in the fourth quarter of the fiscal year, increasing the value available to be recognized as earned revenue in future years.

Deferred Revenue balances as at September 30, 2023

As at September 30, 2023, the City recorded deferred revenue liabilities in the amount of \$7,402.8 million, an increase of \$1,778.9 million from the December 31, 2022 balance of \$5,623.9 million. Major deferred revenue contributions, which are restricted by legislative requirements or contractual terms and conditions, come from:

- Contributions of \$831.0 million in development and planning act contributions from developers to be earned revenue when critical growth-related capital project costs are incurred. Development charges are restricted by the Development Charges Act, 1997;
- Contributions of \$749.5 million from Water and Wastewater rates to be used for the specific provision of water and wastewater services and capital infrastructure; and
- Contributions of \$257.4 million to be used to fund priority infrastructure projects eligible under the Canada Community-Building Fund Program.

The City's capital expenditures are ultimately supported using several different financial arrangements, including revenue recognized in accordance with the underlying legislation or contract supporting the deferred revenue balance. Therefore, the City's deferred revenue balance, on a standalone basis, is insufficient to support capital investment decisions that are made in relation to the City's 10-year capital plan and growth-related assumptions. In particular, the City estimates that \$22.7 billion of deferred revenues have been committed over the 2023-2032 period – this indicates that the City's commitments are 3.1 times greater than the amount of deferred revenues recognized as at September 30, 2023.

Staff will continue to monitor the financial implications associated with legislative changes, such as those introduced by Bill 23, as more information is received from the Province. For instance, Bill 23 is estimated to result in a revenue loss of \$2.3 billion, which includes loss of development charges of \$2.0 billion, over a 10-year period (i.e., 2022-2031). The largest impact is to housing services, which has been removed as an eligible development charges service. This estimate is based on available information from the 2022 development charge background study, which included a development forecast of 136,000 housing units over 2022-2031.

During the nine months ended September 30, 2023, \$131.6 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, 2023, with comparatives at December 31, 2022.

Table 1: Deferred revenues at September 30, 2023 with December 31, 2022 comparatives (\$ millions)

(\$ millions)	Sep. 30, 2023	Dec. 31, 2022
Deferred revenues:		
Restricted by Provincial legislation		
Development charges	3,294.9	2,713.9
Parkland acquisition/new development	892.4	819.5
Planning Act	621.2	522.7
Building Code Act service improvement	242.1	220.6
Provincial Gas Tax revenues for Public Transit	1.0	0.4
	<u>5,051.6</u>	<u>4,277.1</u>
Restricted by agreements with third parties		
Water / wastewater	1,960.0	1,210.7
Third party agreements	269.0	12.9
Community services	66.7	66.6
Toronto Transit Commission	44.5	45.6
State of good repair	9.4	9.4
Parking Authority	1.6	1.6
	<u>2,351.2</u>	<u>1,346.8</u>
Deferred Revenues as at September 30	<u>7,402.8</u>	<u>5,623.9</u>

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, 2023. The City's 10-year Capital Plan estimates that \$22.7 billion has been committed to fund capital works over the 2023-2032 period, with the largest funding commitments coming from Water and Wastewater Capital (\$14.2 billion) and Development Charges (\$6.8 billion).

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SIGNATURE

Stephen Conforti
Chief Financial Officer and Treasurer

ATTACHMENTS

Appendix A: Deferred Revenues as at September 30, 2023