

September 16, 2011

City Debt

- As well as an annual operating budget, the City prepares a 10-year Capital Budget and Plan. This capital plan, based on debt affordability, includes estimates of capital expenditures (capital projects) to keep the City's current assets in a state of good repair and to improve, expand, acquire and/or construct new capital assets required to meet service demands and support service growth.
- The City's Capital Budget pays for building and maintaining roads, TTC buses and subways and major equipment and building major facilities. Major projects are funded through property taxes, money from other levels of government, development fees and by borrowing.
- The City maximizes all non-debt financing sources first to minimize debt funding; these include Federal/Provincial Transfers, Program-specific reserve funds and capital contribution from the operating budget (Capital from Current).

When does the City issue debt?

The City of Toronto Act permits the City to borrow funds (issue debt) to finance capital expenditures, by selling debt to any public investor. Debt funding levels are established for each year of the 10-year capital planning period. Debt repayment (principal and interest) is an operating expenditure which must be managed. The City cannot issue debt for operating expenses and must have a balanced operating budget each year.

The City restricts its debt service cost limit to no more than 15 per cent of property taxes, which means that 85 cents of every tax dollar raised is available for operating priorities.

Debt can provide the City with more affordable financing by matching the repayment term to the economic useful life of the project, instead of funding the entire cost from current revenues. Without debt financing, the entire cost of a project would be borne on current taxpayers. Instead, the repayment term allows future generations, in fairness, to also benefit from the project and contribute to its cost.

In the past year, the City has aggressively paid down portions of its debt and in instances where there is a benefit in rates and returns, issues debt within its 15 per cent limit.

When the City pays the servicing costs of its debt, it is legislated to pay principle and interest which is unlike other orders of government who pay interest only.

New Debt issued on June 2, 2011

On June 2, 2011, the City issued \$350 million 30-year debt to finance capital expenditures approved by Toronto City Council in its 10-year Capital Budget Plan.

Projects funded by today's debt issuance include: the purchase of streetcars for the TTC, LRT Replacement Maintenance and Storage Facility Project, Spadina Subway Extension, Toronto Waterfront Revitalization Initiatives, Purchase of Subway Cars and Union Station Revitalization.

The City's Current Debt Situation

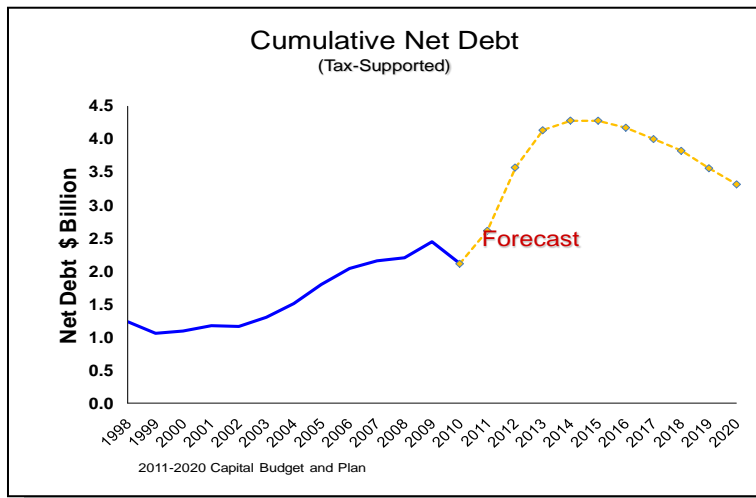
The City borrows to fund capital expenditures. The goal for capital financing is to maximize all funding from external sources, including Federal and Provincial Governments, development charges, donations and reserve funding, before using City's own revenue sources, namely operating contributions "capital from current" and issuance of debt.

Toronto has enjoyed relatively low debt levels; however, in light of the growing capital infrastructure needs, there is a sizeable and growing gap between future capital expenditure needs and ongoing sustainable revenue sources. The City does not have the fiscal capacity for necessary growth related expenditures, e.g. TTC, Transportation, etc. For the next ten years, the TTC is projected to make up the majority of the new debt required to fund the City's capital requirement. In fact, no new debt is required to fund the City's programs except for the TTC by 2014.

Toronto has achieved very high credit ratings of between one and two levels below the highest possible AAA rating. This reflects the rating agencies' views that the City has modest levels of debt, high levels of dedicated reserves, a strong and diverse economy and a well managed organization. As a result, the City's cost of debt is among the lowest of Canadian municipalities.

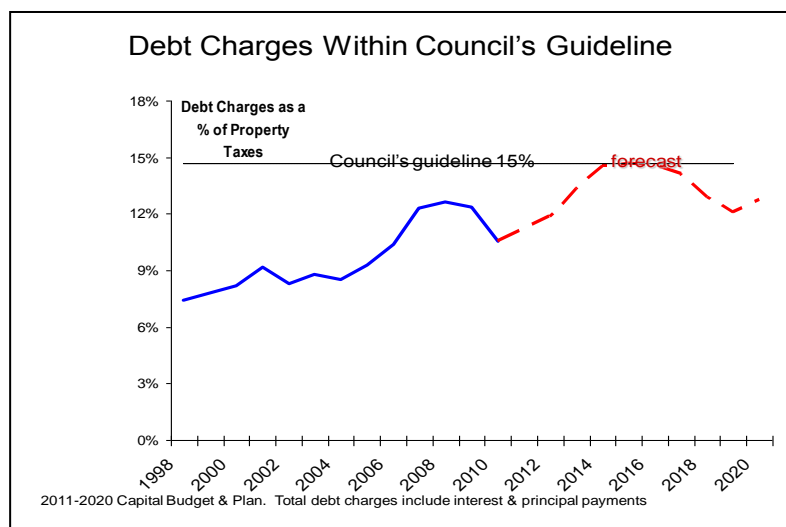
The City has implemented a framework for developing multi-year capital and operating budgets, and ensured that limited resources are aligned to priorities to maximize the benefits for Toronto's residents.

Gas tax funding from the federal and provincial governments, as well as provincial transit capital funding has alleviated some of the capital financing pressures and will help to lessen future debt requirements. To properly fund the capital needs of the City over the next decade, meet affordability guidelines, protect the City's excellent credit rating and take advantage of the very low interest rates now available for longer-term loans, the City in 2010 refinanced parts of its current and future debt by paying down existing debt, and borrowing funds for selected projects on 30-year terms as opposed to the current 10-year term. The 30-year debt was used to finance long term assets such as subway tunnels and subway cars. This means that the period of time for which money is borrowed more closely match the life span of the infrastructure being built or purchased. As part of this debt restructuring approach, the City used the proceeds of the Toronto Hydro promissory note, which had been dedicated to two specific areas of investment (Spadina subway and Waterfront development), and paid down approximately \$600 million of existing debt. The projects previously funded from this reserve were refinanced for that amount over a 30-year period and only when the funds would actually be required. Current estimates showed that the City's net long-term outstanding debentures would increase from \$2.2 billion at the end of 2010 to peak at just over \$4.2 billion in 2015 (mainly due to Pan Am Games and the TTC), and decrease to \$3.4 billion by 2020 as shown in the chart below.

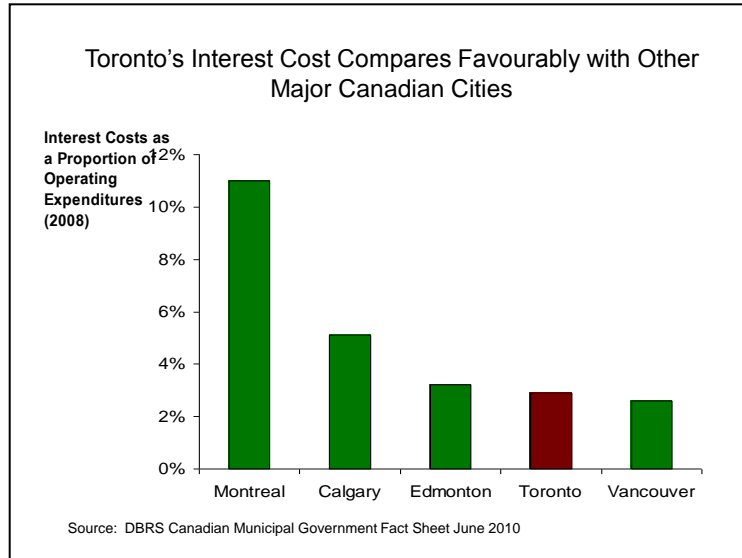


City Council previously approved a debt service guideline such that the debt service cost should not exceed 15 per cent of property tax revenues in a given year. This limit means that at least 85 cents on each tax dollar raised is available for operating purposes.

The debt refinancing strategy will help manage the pressures of debt repayment related to the annual operating budget. Repayment of principal and interest on the City's debt continues to be the second highest expense on the annual property tax bill. Lowering the annual debt payments, and spreading them out over a longer period, will allow the City to direct more property tax dollars to services each year. Current forecasts show that the City's debt charges will be within this guideline in the next few years as illustrated below.



Overall, the City's debt burden is relatively modest and its net tax-supported debt per capita is comparable to other major Canadian municipalities. Interest costs also compared favourably with the other major Canadian municipalities, as illustrated below.



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