TORONTO

STAFF REPORT
ACTION REQUIRED

FINANCING OF CAPITAL WORKS POLICY AND GOALS

Date:	February 20, 2007
To:	Budget Committee and Executive Committee
From:	Deputy City Manager and Chief Financial Officer
Wards:	All
Reference Number:	P:\2007\Internal Services\Cf\bc07008Cf – et (AFS #4184)

SUMMARY

This report requests Council's approval for the City's Financing of Capital Works Policy and Goals in order to fulfill the requirement of paragraph 8 of subsection 212 (1) of the *City of Toronto Act, 2006.*

RECOMMENDATIONS

The Deputy City Manager and Chief Financial Officer recommends that:

(1) Council approves the City of Toronto's Financing of Capital Works Policy and Goals as contained in Appendix A, and

(2) Council authorizes the appropriate City of Toronto officials to take the necessary actions to give effect thereto.

FINANCIAL IMPACT

The key guidelines contained in the "Financing of Capital Works Policy and Goals" are the 15% of the tax levy limit on debt charges and the City's total direct obligation debt which shall not exceed $3.5 billion over the term of Council, ending on November, 2010.

DECISION HISTORY

Paragraph 8 of subsection 212 (1) of the *City of Toronto Act, 2006* (COTA) requires Council to adopt and maintain a policy with respect to the financing of capital works before an agreement to issue debt can be entered into.

ISSUES BACKGROUND

Before the City can issue debt, Council is required to adopt a policy in respect of the financing of capital works and goals that includes requirements pertaining to limits on the amount of debt to be issued annually and limits on the annual costs associated with this financing.

COMMENTS

The attached policy statement in Appendix A satisfies the requirements of the COTA that requires Council to adopt and maintain a policy that addresses the limits for issuing debentures, based upon limits of the associated annual financing costs.

Adherence to the policy will assist the City in achieving the lowest cost of funds, given current capital market conditions, while maintaining the highest possible credit rating through prudent long-term financing planning as well as maintaining the City's reputation as a respected participant in global capital markets.

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SIGNATURE

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Joseph P. Pennachetti
Deputy City Manager and Chief Financial Officer

ATTACHMENTS

Appendix A – City of Toronto Financing of Capital Works Policy and Goals

Appendix A

City of Toronto Financing of Capital Works Policy and Goals

1. Policy Statement

It is recognized that the City of Toronto has a reputation as a respected participant in global capital markets. Adherence to its financing of capital works policy and goals will enhance this reputation and ensure the City's continued access to these markets in order to raise funds through the issuance of debt securities in an efficient and cost-effective manner for the purpose of capital financing.

The City of Toronto is committed to achieving the lowest cost of funds when financing capital works, based upon current capital market conditions. When making decisions regarding the financing of a capital expenditure through the issuance of debt, Council must be satisfied that the lowest cost alternative is utilized from a total cost of funds perspective.

This policy ensures that Council complies with the debt issuance and management provisions contained in the *City of Toronto Act, 2006* (COTA) and its regulations while providing Council with the flexibility to meet the City's annual capital needs during its term-of-office.

The City seeks to maintain the highest possible credit rating. While the City recognizes that external economic, natural or other events may affect its credit rating, it is committed to ensuring that actions within its control are prudent and necessary as they relate to the issuance and management of short and long term debt.

2. Authority and Accountability

Paragraph 8 of subsection 212 (1) of the (COTA) requires Council to adopt and maintain a policy with respect to the financing of capital works before the City can enter into an agreement to issue debt.

For the term of Council, a report requesting the authority for entering into agreements with purchasers for the sale and issuance of debentures to be delegated to the Mayor and the Deputy City Manager and Chief Financial Officer and confirmed by bylaw will be considered by Council. Capital markets require the City to have the ability to act on financing opportunities on a timely and efficient basis in order to secure the best pricing and terms.

3. Debt to be Used Only for Capital Financing

The City is not authorized by legislation and will not issue debt obligations or use debt proceeds to finance current operations.

The City will utilize debt for the acquisition, construction, renovating, repairing or remodeling of capital works where the project cannot be funded from current operating revenues or other sources and where the Deputy City Manager and Chief Financial Officer considers it to be prudent to finance the project over the useful life of the asset.

4. Capital Financing From the Operating Budget

As part of the City's capital financing policies, if economically feasible and determined to be affordable, Council will allocate funds from its operating budget to be contributed to funding capital expenditures on an annual basis which will have the effect of reducing the amount of required financing for capital expenditures.

5. Debt Limits

Provided that the annual costs associated with debt financing shall not exceed 15% of the tax levy, the City shall finance, from time to time, capital works that the City considers necessary or desirable for the public, as included in its Five Year Capital Plan, in accordance with applicable generally accepted accounting principles for local governments as recommended by the Canadian Institute of Chartered Accountants. The budgeted debt charges that will be incurred due to debt issuance will be included in the annual Operating Budget.

The annual costs associated with debt financing shall not exceed 15% of the tax levy and the City's total direct obligation debt shall not exceed $3.5 billion over the term of Council, ending on November, 2010.

The limit is subject to various factors such as the debt requirements contained in the capital budget, new projects that may not be contained in the approved capital budget but arise through events that could not have been foreseen, spending rates that affect capital project completion, the amount of unfinanced capital and capital market conditions such as the level of interest rates.

6. Short-term Borrowing for Capital Purposes

Since it is the City's practice to temporarily finance its capital expenditures from working capital until it is permanently financed, there are occasions when the City must borrow funds to finance these obligations on a short-term basis.

Council will enact a multi-year temporary borrowing bylaw that will authorize short-term borrowing for a capital project up to an amount approved by Council and will cover their term-of-office.

7. Credit Ratings

The City seeks to maintain the highest possible credit rating that can be achieved without compromising the delivery of services and programs through prudent budgetary and debt management policies and procedures.

The City believes that it enhances its ability to issue debt in the global capital markets when the lowest cost of funds is achievable by being rated by the following rating agencies on a continuous basis:

Moody's Investor Service
Standard and Poor's
Dominion Bond Rating Service

8. Long-term Financial Planning

To enhance the credit rating and prudent financial management, the City will conduct long-term financial planning through the adoption of a five-year capital plan and a long-term fiscal plan that will disclose the amount of debt and its projected cost that will be required to finance capital expenditures over the term of Council.

9. Debt Maturities

Under the COTA, the allowable maximum term for debt issuance is 40 years or the useful economic life of the asset, whichever is less.

Debt will be structured for the shortest term-to-maturity consistent with budgeted affordable annual payments of principal and interest and an appropriate allocation of costs to current and future taxpayers.

10. Debt Structures

Debt should be structured to achieve the lowest net cost of funds, given the constraint of debt maturities and current capital market conditions. To the extent possible, the City will structure its debt obligations to require repayment as soon as feasible so as to recapture its borrowing capacity for future use and minimize costs where possible.

Sinking Fund Debt

Under the COTA, the City is authorized to issue debt that requires an annual payment to be made to a sinking fund controlled by the Sinking Fund Committee so that these contributions, when invested at an actuarial interest rate, will provide for the repayment of the debt at maturity. The Committee is comprised of four citizen members with specialized expertise and knowledge that supports and contributes to the quality of the investment management of these funds and the Deputy City Manager and Chief Financial Officer as Chair of the Committee.

The citizen members are appointed by City Council and the Committee has the sole authority for managing the sinking funds' investments and administrative policies.

Installment Debt

Under the COTA, the City is authorized to issue debt that will mature in a given year on an installment or serial basis whereby the principal portion of the debt becomes due and according to a repayment schedule that was established when the debt was issued.

Variable versus Fixed Debt Issuance

Under the COTA, the City may issue up to 10% of its outstanding debt in the form of variable rate debt where the interest rate fluctuates according to a pre-determined formula or benchmark rate such as a Treasury Bill or Government of Canada bond. This type of debt should only be issued if market conditions provide an opportunity for the City to lower its borrowing costs while maintaining the ability to convert the debt into a fixed interest rate if warranted by future capital market conditions.

Re-opening of a Debt Issue

The City will reserve the right to re-open a debenture that has previously been issued and increase its par value if this provides a lower cost of funds than other available borrowing alternatives while increasing the size and liquidity of the original debt issue and broadening the City's investor base.

Bank Loans

As a source for financing capital works, the Deputy City Manager and Chief Financial Officer shall consider bank loans and recommend to Council that it enters into bank loan agreement if it conforms to this policy and achieves the goals of providing a lower cost of funds and flexible terms than other available debt instruments.

Construction Financing

In order to match projected debt charges with future revenues that will be generated after a facility is constructed and operating, the City may issue construction financing whereby the interest or principal payments or both can be deferred up to five years before payment is required. The Deputy City Manager and Chief Financial Officer will recommend this financing for Council's approval if it is determined to be in the best interests of the City.

11. Revenue Bonds

The issuance of revenue bonds will be addressed by a statement that will amend this policy when available.

12. Derivatives and Hedging

The use of derivatives and hedging as related to the issuance of debt will be addressed by a statement that will amend this policy when available.

13. Accessing Capital Financing Programs Offered by Other Levels of Government

When evaluating whether to participate in a loan or debt program being offered by the federal or provincial levels of government, the interest rate and terms will be compared to the City's all-in cost of borrowing and the program must provide a lower cost of funds and competitive terms in order to be considered.

14. Issuing Debt on Behalf of another Jurisdiction

If the City is requested by the Toronto District School Board or the Toronto Catholic School Board to issue debt on their behalf, Council will consider the request as it affects the City's overall borrowing program and deal with the report on a timely basis.

The authority for Council to consider a request and the City's authority to issue the debt is contained in the following section 246 of the Act.

> *"The City may borrow money for the purposes of a school board if the school board exercises jurisdiction in all or part of the City and requires permanent improvements as defined in subsection 1 (1) of the* Education Act*. 2006, c. 11, Sched. A, s. 246."*

15. City Legal Support

Council must adopt a specific borrowing bylaw authorizing the issuance of debentures or the entering into a bank loan for the purpose of capital financing that is covered by this policy.

The City Solicitor provides legal advice with regards to the City debt financing transactions and, in the opinion of the City Solicitor, should the scope of the proposed transaction require, recommend to Council that legal advice be obtained from an independent source. This advice would cover the initial proposal and extend to the various contracts and agreements that would have to be executed in conjunction with the transaction.

The debt issuance syndicate is responsible for retaining external counsel who provides the legal opinion for the investors.

16. Reporting and Disclosure Requirements

The Deputy City Manager and Chief Financial Officer shall prepare and present to the Council a detailed report per the requirements of Ontario Regulation 610/06 of the City of Toronto Act 2006, "Financial Activites". This applies to outstanding debt issued under clause 7(1)(d) of 2(d) of the regulation which relate to construction financing debt where the payment of interest, principal or both are deferred during the period of construction.

"*(1) If the City has any outstanding debt under clause 7 (1) (d) or (2) (d) in a fiscal year, the treasurer shall prepare and present to the council once in that fiscal year, or more frequently if the council so provides, a detailed report on all of that debt. O. Reg. 610/06, s. 16 (1).*

(2) The report under subsection (1) shall contain,

(a) a description of the estimated proportion of the total debt of the City under clause 7 (1) (d) or (2) (d) to the total long-term debt of the City and a description of the change, if any, in that estimated proportion since the previous year's report;

(b) a statement by the treasurer as to whether, in his or her opinion, all debt under clause 7 (1) (d) or (2) (d) of the Act was issued in accordance with the statement of policies and goals relating to construction financing adopted by the City;

(c) an update of the detailed estimate made under clause 15 (2) (c) with respect to the terms of the City's expectations of revenue generation from the undertaking;

(d) a record of the date of the repayment of each instalment of principal, interest or both principal and interest made during the period of construction of the undertaking for which the debt under clause 7 (1) (d) or (2) (d) was issued;

(e) a statement of the outstanding instalments of principal, interest or both principal and interest repayable during the currency of the debt issued under clause 7 (1) (d) or (2) (d) that will be due and payable in each year; and

(f) such other information as the council may require or that, in the opinion of the treasurer, should be included. O. Reg. 610/06, s. 16 (2)."

The report, if required, shall be presented to Council on an annual basis after the end of the City's fiscal year after the City's accounts are closed.