



## STAFF REPORT ACTION REQUIRED

### Use of City Proceeds from Sale of Toronto Hydro Telecom Inc.

<b>Date:</b>	June 17, 2008
<b>To:</b>	Executive Committee
<b>From:</b>	Deputy City Manager and Chief Financial Officer
<b>Wards:</b>	All
<b>Reference Number:</b>	P:\2008\Internal Services\Cf\ec08022Cf – et (AFS #8021)

#### **SUMMARY**

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On Friday June 13, 2008 Toronto Hydro Corporation announced the sale of its wholly owned subsidiary, Toronto Hydro Telecom Inc. As the sole shareholder of Toronto Hydro Corporation, the sale will entitle the City to a one time increase in dividends. In keeping with Council policy and the City's fiscal objectives, the resulting funds should be invested in long term assets of the City.

The City's social housing stock has a well documented and growing backlog of capital maintenance requirements that are affecting the quality of life of the residents, and for which no viable funding source has been identified. The most recent estimate of the cost of this backlog is \$300 - \$350 million, notwithstanding the \$500 million invested from 2002 – 2007, and the planned investment of \$400 million over the next 5 years.

The use of the City's portion of the proceeds from the telecom sale for the rehabilitation of housing stock makes good financial sense for the City - reducing the impact of future debt costs and addressing important infrastructure needs. This report recommends that the City's proceeds from the sale be contributed to a new reserve fund to address the capital backlog of the Toronto Community Housing Corporation (TCHC).

The Province of Ontario has also recognized the repair of housing stock as a priority. On March 31, 2008 the Government announced a budget allocation of \$36.459 million to the City of Toronto for this purpose.

## **RECOMMENDATIONS**

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### **The Deputy City Manager & Chief Financial Officer Recommends that the City:**

1. Request that the Board of Directors of Toronto Hydro Corporation declare a one time special dividend of \$75 million from the net proceeds of the sale of THTI.
2. Establish a new account within the State of Good Repair Discretionary Reserve Funds account, called the Toronto Community Housing Corporation State of Good Repair Reserve Fund, and accordingly:
  - a. amend Municipal Code Chapter 227 (Reserves and Reserve Funds) by adding the Toronto Community Housing Corporation State of Good Repair Reserve Fund to Schedule #8 - State of Good Repair Discretionary Reserve Funds;
  - b. adopt Appendix 1, which describes the purpose and administrative features of the new Reserve Fund.
3. Contribute one time City proceeds resulting from the sale of Toronto Hydro Telecom Inc. by Toronto Hydro Corporation to the new reserve fund as referred to in Recommendation 2.
4. Authorize and direct the appropriate City officials to take the necessary action to give effect thereto and grant leave for the introduction of any necessary bills in Council.

### **Implementation Points**

The declaration of any dividend related to the sale of Toronto Hydro Telecom Inc. (THTI) will be determined by the Board of Directors of Toronto Hydro Corporation.

### **Financial Impact**

Consistent with the recommendations in this report it is expected that a dividend of approximately \$75 million will be attributable to the sale of THTI.

The recommendations would assist 2009 budget deliberations to help address the capital repair backlog of the Toronto Community Housing Corporation, the wholly owned subsidiary of the City of Toronto. The funds would in part offset future TCHC subsidy requirements related to debt and help reduce future capital maintenance expenditures associated with the backlog of capital maintenance.

### **DECISION HISTORY**

In a separate report on this agenda entitled Agreement between Toronto Hydro Telecom Inc. and the City of Toronto for the Provision of Telecommunication Services, the Deputy City Manager and Chief Financial Officer has recommended certain contractual arrangements that would protect the City's telecom service interests and clarify the

relationship between the City and THTI, in anticipation of the potential sale of Toronto Hydro Telecom Inc.

The sale of THTI was announced by Toronto Hydro Corporation on June 13, 2008.

## **ISSUE BACKGROUND**

The sale of THTI is expected to result in an increased dividend to the City, which, unless the recommendations of this report are adopted, would contribute to general revenues and fund the operating budget. Accordingly, the Mayor announced on June 13, 2008, that he would seek the support of Council to contribute these funds to a capital reserve for the purposes of addressing the capital backlog of TCHC. This report provides the means for Council to consider such a policy.

## **COMMENTS**

### Optimization of Assets

In February 2008 the Mayor's Fiscal Review Panel Final Report "Blueprint for Fiscal Stability and Economic Prosperity" recommended a review of capital assets, specifically:

- evaluate all options for maximizing the value of the City's major capital assets (including Toronto Hydro)
- ensure that the proceeds be used to reduce existing debt or offset future needed borrowing
- review partnerships with outside stakeholders...[to get]....a better return in its investments

The sale of Toronto Hydro Corporation's telecom subsidiary is consistent with these recommendations. It takes advantage of the current strong market for these assets, maximizing the value of the asset and the returns to the Corporation, while avoiding future debt requirements and risks associated with continuing to build the business. The sale also enhances THC's ability to invest in the renewal of its core distribution system business. The City's use of its proceeds from the sale to help reduce the TCHC social housing capital backlog also reduces the need to rely on debt, and the investment would help reverse any further deterioration of the value of these housing assets.

### Shareholder Direction

Toronto Hydro Corporation operates under the Ontario Business Corporations Act and the City's Shareholder Direction. The Direction allows the Corporation to sell its subsidiaries but not all or substantially all of its assets. The sale of Toronto Hydro Telecom Inc. represents a small portion of the consolidated assets of the corporation, and so is consistent with the Shareholder Direction.

The Direction also sets out the shareholders expectations for declaration of dividends, at a rate of 50% of the annual corporate consolidated net income each year paid in fixed

quarterly installments summing to \$25 million, with any balance paid within 10 days of approval of the annual financial statements.

This report recommends that the Board be requested to declare a special dividend of \$75 million based on the net proceeds of the sale, in recognition of the fact that that sale converts the investment in the telecom subsidiary to cash, and therefore allows a higher dividend rate in this circumstance. The remaining normal dividend calculation for the year would be based on 50% of net income excluding the impact of the sale.

### TCHC Requirements

Since the Provincial government downloading of social housing costs in 1998 and the devolution of social housing assets and liabilities to the City of Toronto as municipal service manager in 2002, the capital maintenance burden of the housing stock has been better quantified, and is not affordable within historical budgetary envelopes. TCHC estimates its capital backlog at between \$300 and \$350 million, notwithstanding the \$500 million invested from 2002 – 2007, and the planned investment of \$400 million over the next 5 years.

The Government of Ontario recognized this problem in its 2007/08 Budget by making a \$100 million allocation to social housing capital repairs across Ontario. The City of Toronto share of this funding of approximately \$36 million is scheduled to be received by June 30, 2008. The recommended use of the Provincial grant is dealt with in a separate report to the July 4 meeting of Community Development & Recreation Committee. The grant represents only about 10% of the TCHC backlog, so substantial funding requirements will remain.

### Impact of Recommendation

The recommended contributions to a new Social Housing State of Good Repair Reserve Fund will help address the TCHC capital repair backlog and enable more work to be done on a faster timetable, with less reliance on debt. The investment will help improve conditions for the tenants, and should have the added effect of reducing operating costs as well as avoiding additional debt service costs.

Toronto Community Housing Corporation forecasts that the current level of capital repair expenditure cannot be maintained past 2009 without new funds being identified. The use of the City's portion of the proceeds from the sale for the rehabilitation of housing stock makes good financial sense for the City - reducing the impact of future debt costs and addressing important infrastructure needs.

It is estimated that the new funds would allow Toronto Community Housing to accelerate the refurbishing of 5,000 more units of housing, and retrofitting 10 buildings with new energy efficient building systems.

Actual expenditure plans and withdrawals from the reserve would be considered as part of the 2009 budget process.

## **CONTACT**

Len Brittain, Director, Corporate Finance Division, 392-5380, lbrittai@toronto.ca

## **SIGNATURE**

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Deputy City Manager and Chief Financial Officer

## **ATTACHMENTS**

Appendix 1 - The Toronto Community Housing Corporation State of Good Repair Reserve Fund

## **Appendix 1**

### **The Toronto Community Housing Corporation State of Good Repair Reserve Fund located in Schedule #8 - State of Good Repair Discretionary Reserve Funds**

1. Purpose: The Toronto Community Housing Corporation State of Good Repair Reserve Fund will provide capital funds for the maintenance of existing housing stock owned by the Toronto Community Housing Corporation
2. Service Area or Beneficiary Program: The Toronto Community Housing Corporation will be the beneficiary of funds from the Reserve Fund
3. Initial Contribution: None.
4. Contribution Policy: Upon receipt of an anticipated special dividend from Toronto Hydro Corporation related to the sale of its telecom subsidiary, a contribution of \$75 million would be made.
5. Withdrawal Policy: Funds will be transferred to the Toronto Community Housing Corporation to assist in the capital maintenance of owned housing stock including energy efficiency improvements via approved budgetary allocations.
6. Review Cycle: Once the funds have been exhausted, the Reserve Fund will be closed. If in five years funds still remain, the purpose of the reserve fund should be reviewed.