STAFF REPORT
ACTION REQUIRED

Loss of Toronto Pooling Compensation for Social Housing – Budget Strategy

Date:	January 29, 2015
To:	Budget Committee
From:	City Manager Deputy City Manager & Chief Financial Officer
Wards:	All
Reference Number:	P:\2015\Internal Services\Cf\Bc15003Cf (AFS #20813)

SUMMARY

In 2008 the Province initiated a Toronto Pooling Compensation program to compensate the City for the termination of GTA Equalization ("pooling") payments and Ontario Municipal Partnership Fund (OMPF) grants formerly provided to mitigate the disproportionate cost of downloaded housing and social service costs borne by the City.

In June 2013 the Province unexpectedly announced the phase-out of Toronto Pooling Compensation over three years, from 2014 to 2016, creating a $129 million annual revenue shortfall by 2016. In 2014 the City funded the first $43 million shortfall with one time sources. In 2015 the shortfall is $86 million.

On January 19, 2015 the province indicated that it would facilitate a short term lending program to assist the City with the phasing-out of the grant. This report describes the results of discussions with the province, and how staff propose to address the situation.

RECOMMENDATIONS

The City Manager and the Deputy City Manager & Chief Financial officer recommend that:

1. This report be received for information.

Implementation Points

In order to address the revenue shortfall, the City must begin implementing expenditure reductions and/or tax increases. Following discussion of various options, the province offered a short term capital line of credit to the City, which would facilitate a strategy to temporarily reduce capital from current financing (in the operating budget) to cover the interim operating shortfall while permanent budgetary adjustments are phased-in over a maximum of six years. The loan would be for capital purposes because municipalities cannot borrow to cover operating deficits.

For various reasons discussed in this report, staff believe that it is in the City's interest to develop an in-house City strategy, based on the approach discussed with the province, but using traditional borrowing methods such as bank loans to achieve a similar result, as described herein.

Financial Impact

In 2008, in recognition of the phase-out of both GTA Equalization ("pooling") and the Ontario Municipal Partnership Fund, the Province announced a special grant for the City. The amount of the grant changed annually according to a schedule that reflected both cost uploading and related funding losses. By 2018, the grant amount would be adjusted to $115 million annually, the amount associated with funding the City's disproportionate cost of social housing.

The cancellation of the grants announced in 2013 was spread over a three year period. The difference between the two schedules and the impact on the City budget is illustrated in the table below, from the July 16, 2013 Council report.

TABLE 1: PROVINCIAL FUNDING (TORONTO POOLING COMPENSATION) REDUCTION

$ Millions	2013	2014	2015	2016	2017	2018
Scheduled TPC Payments	149.3	142.5	135.6	128.8	121.9	115.1
Revised Plan	149.3	100	50	0	0	0
Cumulative Impact	0	(42.5)	(85.6)	(128.8)	(121.9)	(115.1)
Cumulative Property tax impact		1.8%	3.6%	5.4%		
Incremental Impact		(42.5)	(43.1)	(43.2)		
Incremental Property Tax Impact (original 2013)		**1.8%**	**1.8%**	**1.8%**		
Incremental Property Tax Impact (updated 2015)		**0.0%**	**3.4%**	**1.7%**		

In 2013 City Council responded by requesting the Province rescind its decision to eliminate Toronto Pooling Compensation by 2016 or, at a minimum, maintain the social housing component of Toronto Pooling Compensation.

The City's 2014 Budget addressed, on a temporary, one time basis, the first tranche of Toronto Pooling Compensation loss by applying the financial proceeds of a concurrent action by the province to cancel the City's residual amalgamation transition loan. This budget measure provided time for the City to petition for relief from the grant termination, but did not address the revenue loss. After numerous discussions with provincial officials, the result is an offer of a short term financing facility from the province, as described here-in.

Some combination of expenditure reductions and/or revenue increases will be required to fully address the loss of the funding. Using a financing strategy similar to the one discussed with the province, taking advantage of the current low interest rates, the City can spread the budgetary adjustments over a more manageable period. Phase-in options and specific 2015 impacts will be recommended in a subsequent report to Budget Committee.

DECISION HISTORY

The province's decision to terminate Toronto Pooling Compensation over three years was communicated to City Council in a report at its July 16, 2013 meeting (see link below).

http://app.toronto.ca/tmmis/viewAgendaItemHistory.do?item=2013.CC37.5

ISSUE BACKGROUND

Toronto provides 90% of the public housing in the GTA and 37% of the total social housing in the Province, but comprises only approximately 20% of the Province's population.

	Toronto	GTA	Ontario	Toronto %	
				GTA	Ontario
Population (2011)	2,615,060	6,054,191	12,851,191	43.2%	20.3%
Public Housing	43,869	48,434	99,331	90.6%	44.2%
Other (Non-Profits/Co-ops)	51,797	77,842	157,429	66.5%	32.9%
TOTAL	**95,666**	**126,276**	**256,760**	**75.8%**	**37.3%**

For these reasons the transfer of responsibility for social housing to municipalities placed a disproportionate burden on the City. This burden was initially mitigated by GTA Equalization, and later by Ontario Municipal Partnership Fund eligibility, and most recently by Toronto Pooling Compensation. The termination of the funding was accompanied, and initially offset in part, by the cancellation of Toronto's amalgamation Transition Loan.

COMMENTS

As a result of recent discussions with the province, it has become clear that an interim financing and phase-in option is the City's remaining viable option.

It is now appropriate for the City to begin to identify and implement a permanent solution to the revenue loss associated with the phase-out of the funding. Since the cost is significant, i.e. equivalent to a 5.1% residential tax increase by 2016, it is reasonable to consider financing a phase-in of impacts as contemplated in discussions with the province. Phase-in of the budget adjustment could balance the need to take time to achieve expenditure reductions and/or gradually increase tax rates, while minimizing financing costs and taking advantage of low short term interest rates.

Municipalities may only borrow for capital purposes. However, the City could finance a portion of the capital expenditures typically funded through capital from current (CFC). The resulting operating budget room from temporarily reduced CFC could fund the housing shortfall until permanent measures are in place. The financing would be of a short term nature, lasting no more than 4 to 6 years.

Terms of Provincial Offer of Assistance

As a means of helping the City adjust to the loss of the grants, the province offered to provide the City with a secured, short term capital line of credit. The line of credit would provide replacement capital financing to offset temporary reductions in capital from current contributions. The credit would be available for four years, by which time sufficient operating budget adjustments would be implemented to offset both the funding loss and the debt repayment over a maximum of six years.

The provincial offer includes interest rates on full commercial terms (i.e. higher than the Province's own cost of borrowing) plus security requirements including pledged property assets, an explicit right to claw back gas tax entitlements in the event of default, and potential advanced repayment in the event of budget surpluses.

In addition, amendments to provincial regulation would be required to provide sufficient authority for the City to accept a provincial loan in the form of short-term financing that is not required to be replaced with longer-term debt, and to permit the City to pledge land as security for the debt as requested by the Province.

The City already has strong liquidity and access to capital financing, with no special security requirements or regulatory changes. Following detailed review of the provincial offer, it was determined that the City would be better served by seeking market based financing on standard municipal terms.

Proposed Strategy - Traditional City Financing

Section 3 of Ontario Regulation 610/06 under the City of Toronto Act allows the City to borrow for capital purposes either through issuance of debentures, or bank loans. Bank loans may offer greater flexibility in terms of borrowing and repayment schedules, and therefore are most suitable for providing short term financing. For example, bank loans may allow for early repayment in the case where the City identifies budget adjustments ahead of expectations. In either case, interest rates are at historic lows, minimizing the cost associated with short term borrowing.

No further authority is required for the City to enter into a bank loan agreement, provided that (i) the loan agreement requires some repayment of principal and interest each year; (ii) total variable rate bank loans do not exceed 15% of outstanding City borrowing; and (iii) the City does not provide security as collateral for the loan.

It is vital that any reduction to capital from current to be replaced by increased borrowing be for a short and temporary adjustment period. Capital from current growth is a critical part of the City's long term fiscal plan (as is the debt service ratio limit). The phase-in option is only being considered due to the extreme and unavoidable nature of the budget impact associated with the social housing funding changes.

It is also important to consider that the longer it takes to implement budgetary changes, the more interim financing is required to make up the funding shortfall, and these funds will need to be repaid with future revenues. So in addition to a short budget phase-in period, adjustments should begin in 2015 if possible. Under the provincial credit offer borrowing would have been limited to four years, and repayment within six years. Staff would consider these upper limits. With these parameters, potential budget impacts in any one year could be kept to the equivalent of a 2% tax impact or less.

The additional debt repayments, although interim and not part of the City's normal debenture financing program, would temporarily increase the City's debt service-to-tax revenue ratio, depending on the schedule of budget adjustments and debt repayments. Therefore, if implemented, staff may need to propose further adjustments to the preliminary capital expenditure or financing plan.

SUMMARY

Staff will report back to Budget Committee with a short term financing mechanism, potential phase-in options, and possible budgetary adjustments for the 2015 operating budget to mitigate or eliminate any potential 2015 tax increase.

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