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Region of Peel
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**REPORT**
**Meeting Date: April 25, 2013**
**Regional Council**

DATE: March 22, 2013

REPORT TITLE: **2013 DEBENTURE BORROWING**

FROM: Norma Trim, Chief Financial Officer and Commissioner of Corporate Services

## RECOMMENDATION

**That the Chief Financial Officer and Commissioner of Corporate Services ("CFO") be authorized to negotiate a debenture issue(s) in a principal amount not to exceed $300 million in 2013 and not to exceed a term of 21 years;**

**And further, that the CFO be authorized to negotiate an additional debenture issue(s) in a total principal amount not to exceed $50 million in 2013 on behalf of the City of Mississauga and $3 million in 2013 on behalf of the Town of Caledon not to exceed the term years approved by their respective Councils;**

**And further, that the CFO be authorized to negotiate an additional debenture issue(s) in the principal amount not to exceed $50 million in 2013 and not to exceed a term of 40 years for Social Housing project(s) financing to replace internal borrowing for the Chapelview and Creditvale Mills projects.**

### REPORT HIGHLIGHTS

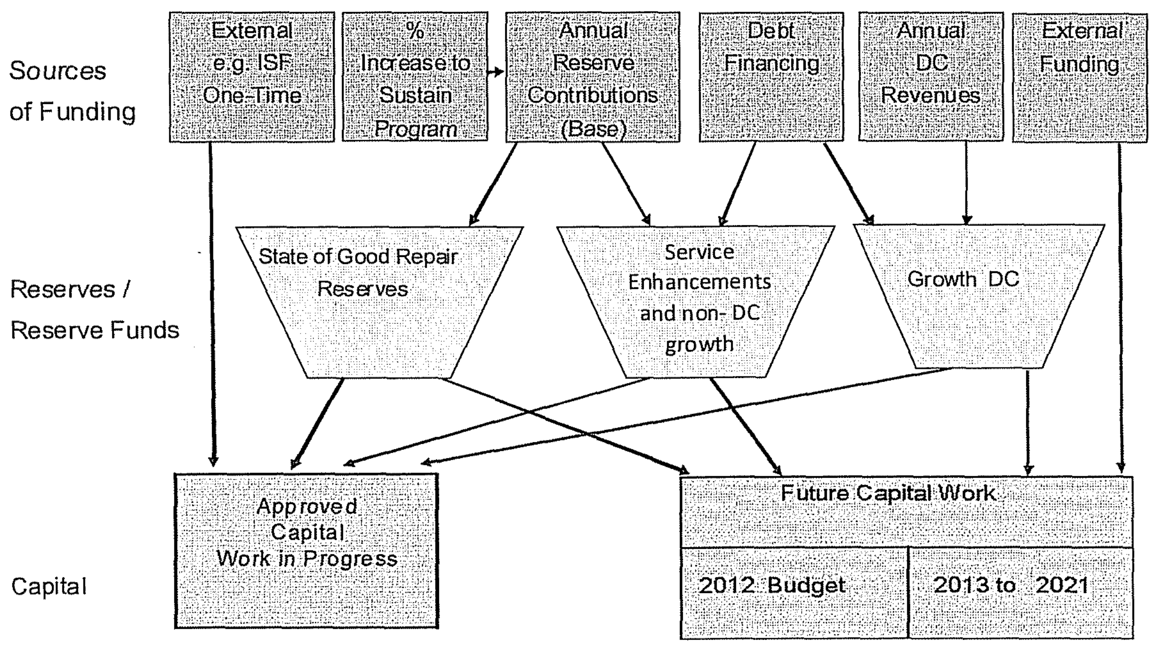
- As reported to Regional Council in 2012 during the update to the Development Charges By-law, Development Charges (DC) funded projects will require borrowing of up to $2.6 billion due to the requirement that Regional infrastructure (primarily for water and wastewater) needs to be constructed in advance of land development and the collection of development charges.
- Borrowing for development charge funded projects is required in 2013.
- Borrowing rates remain at near historic lows which continues to make this an opportune time to secure long-term financing.
- Smart use of long-term debt is necessary to protect the Region's strong liquidity position and to maintain its AAA credit rating going forward.
- The City of Mississauga has requested debenture financing not to exceed $50 million, while the Town of Caledon has requested financing of an amount not to exceed $3 million.
- The Region's debt policy allows Social Housing projects to incur debt for up to 40 years, which is the maximum under the *Municipal Act, 2001* but less than the 50 years the provincial government typically issued debentures for on housing projects.
- Past 50 year mortgages for social housing have had interest rates of up to 9.5 per cent compared to current 40 year rates around 4 per cent.
- The John Street (Chapelview) project explicitly authorizes the Treasurer to negotiate external debentures to replace internal borrowing while Council can approve the securing of low external rates for the Creditview/Eglinton (Creditvale Mills) project.

## DISCUSSION

### 1. Background

Since the 2007 DC Bylaw update, Council has been aware of the need to issue debentures primarily to fund the significant expansions planned to the water and wastewater systems. In 2012, the CFO provided reports to Council such as the "2012 Development Charges Study – Preliminary Findings", dated March 29, 2012 and "Final 2012 Development Charges By-Law", dated September 10, 2012, as well as presentations on the Development Charges By-law update. These reports and presentations highlighted that due to the requirement that Regional infrastructure (primarily for water and wastewater) be constructed in advance of land development and the collection of development charges, borrowing of up to $2.6 billion will be required for DC funded projects. This multi-year borrowing will end and the debt will be paid down in subsequent years as DC expenditures moderate and DC revenues grow.

<u>2013 Capital Plan Management</u>
The sustainability of the Regional capital program requires a multi-faceted approach. As part of previous budget presentations, Council was reminded of the comprehensive strategy to manage the Capital Plan (see following figure).




<u>Maintaining Credit Rating</u>
It is this comprehensive approach to capital sustainability and reserve management which has allowed the Region to consistently achieve an AAA credit rating. In our most recent reviews, both Standard & Poor's (S&P) and Moody's Investment Services reconfirmed the Region's AAA status. Both agencies have maintained a stable outlook for the Region reflecting the expectation that Peel's economy will not encounter a prolonged slump and that Peel will continue to maintain strong cash and liquid investment balances. Not meeting

these expectations could trigger a reconsideration of the Region's credit rating possibly resulting in a lower rating in the future, which would impact the cost of debt going forward.

At the time of writing this report, liquid investments totalled $1.7 billion. Liquid investments that can quickly be converted to cash are important to pay for unexpected expenses like H1N1, to take advantage of opportunities like infrastructure stimulus funding, to phase-in shocks such as the impacts of economic downturns and from a credit rating agency standpoint, to assure investors that the Region has sufficient cash to fund the next year's debt payments.

**2. Proposed Direction**

Smart Use of Debt

The smart use of debt is an effective management tool long utilized by competitive and profitable businesses. Businesses often utilize debt to leverage return on investments in order to benefit shareholders. Through periods of growth, businesses will utilize debt to fund the acquisition of major capital assets so as not to impinge upon working capital, which could hamper day-to-day operations.

It is recommended that authorization be given for the Region of Peel to issue debentures in 2013 of up to the maximum of $300 million and a maximum term of 21 years. This level of debt is well within the Region's revised Annual Debt Repayment Limit.

In addition, the Region has received requests for debenture financing from the City of Mississauga for a total amount not to exceed $50 million and from the Town of Caledon for an amount not to exceed $3 million.

Social Housing Borrowing

While it is unclear what level of liquidity Moody's and S&P consider adequate to maintain our credit rating, if the Region does not issue debt this year, the Region can expect a further draw-down against cash and liquid investments of a forecasted $200 million.

Funding requirements for repair and replacement of assets in the capital plan are currently forecasted to exceed internal reserves balances over the next 10 years. Council has therefore endorsed a strategy to bolster replacement reserves through dedicated increases of 1 per cent for tax and 6 per cent for water & wastewater.

The use of reserves to internally fund the John Street (Chapelview) project was identified as a temporary measure with explicit authority provided to the Treasurer to "conduct negotiations for external financing to replace internal loans subject to Council approval" as approved in the joint report of the Commissioner of Housing and Property and General Manager, Peel Living and the Treasurer and Commissioner of Finance, dated August 22, 2003, titled "John St. Update – Long-term Financing Requirements and Impact on Current Operational Budget, City of Brampton Ward 3". The Creditview/Eglinton (Creditvale Mills) project also has internal funding that Council may authorize to be replaced with external debt. Since 2003, Government of Canada 30 year bond rates have declined over 300 basis points (3 per cent).

The Region's debt policy allows Social Housing projects to incur debt for up to 40 years, which is the maximum under the *Municipal Act, 2001*. According to Ministry of Municipal Affairs and Housing documentation, the provincial government typically issued debentures for 50 years for their social housing projects. Past 50 year mortgages for social housing have had interest rates of up to 9.5 per cent compared to current 40 year rates around 4 per cent. Both in 2011 and 2012 we noted that several other Canadian municipalities issued debt with a 40 year term. The market for such debt is quite narrow, as there are a limited number of investors that are active in this market. The timing of such an issue is dependent upon market demand.

Given the need to maintain liquidity in the reserves, the low rates and strong investor interest shown in a 40 year Region of Peel debenture, the Treasurer is recommending that in addition to the above authorizations, external debt of up to $50 million for up to 40 years be secured for both of these internal social housing loans.

Benefits of Issuing Long term Debt
The likely benefits of retaining the flexibility to issue bonds for up to a 40 year term include the following:

- interest rates continue to be at near historically low rates, a very favorable scenario to lock in rates at these levels;
- with longer term debt, annual debt charges would be significantly lowered during the life of these bonds; and
- while the market generally favours 10 year (short) and 30 year (long) terms, some investors, notably liability driven investors (e.g. life insurance companies), seek out longer terms for a portion of their investable funds. It is therefore recommended that for Social Housing projects, 40 year term of debt be sought which would more closely match the useful life of the asset(s).

## CONCLUSION

Council has been made aware of the pending need to borrow funds to offset anticipated cash flow shortfalls in DCs. The issuance of external debt is an effective means by which the Region can fund its borrowing requirements. In order to preserve Peel's credit rating and take advantage of historically low interest rates, the timing is now appropriate for Council to authorize the Region of Peel to issue debentures.

Norma Trim
Chief Financial Officer
and Commissioner of Corporate Services

**Approved for Submission:**

David Szwarc

D. Szwarc, Chief Administrative Officer

*For further information regarding this report, please contact David Bingham at extension 4292 or via email at dave.bingham@peelregion.ca*

*Authored By: Paul L. Pohl*