

LATE DISTRIBUTION FOR COUNCIL - DECEMBER 15, 2009

A16



ADMINISTRATIVE REPORT

Report Date: December 10, 2009
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Meeting Date: December 15, 2009

TO: Vancouver City Council
FROM: Director of Finance / General Manager of Financial Services Group
SUBJECT: Debenture Program - 2010

RECOMMENDATION

A. *THAT, under authority granted by Section 242(2)(b.1) of the Vancouver Charter, Council approve borrowing authority of \$15 million related to the Southeast False Creek Neighborhood Energy Centre.*

B. *THAT, subject to approval of Recommendation A, Council authorize the issuance of up to \$140 million City of Vancouver debentures utilizing borrowing authority approved as part of the 2008 and 2009 Capital Budgets and through special approvals as follows:*

• <i>Waterworks</i>	<i>\$ 21,600,000</i>
• <i>Sewers & Drainage</i>	<i>\$ 25,000,000</i>
• <i>Neighborhood Energy Utility</i>	<i>\$ 15,000,000</i>
• <i>Public Works</i>	<i>\$ 33,275,000</i>
• <i>Parks & Recreation</i>	<i>\$ 25,000,000</i>
• <i>Community Legacy Projects</i>	<i>\$ 1,125,000</i>
• <i>Public Safety & Civic Facilities</i>	<i><u>\$ 19,000,000</u></i>
	<i><u>\$140,000,000</u></i>

C. *THAT, until the borrowing authority established pursuant to Recommendation B is exercised, the Director of Finance, in consultation with the Mayor, the Chair of the City Services and Budgets Committee, and the City Manager, or a majority of them, be empowered to act and instruct the City's Fiscal Agent to proceed with the issuance of the debentures, and to set the rate, price, and other terms and conditions on which the debentures will be issued by the City.*

It should be noted that once the Director of Finance instructs the Fiscal Agent to offer the debentures in the public market, Council will be required to enact the appropriate borrowing by-law to authorize issuance of the debentures.

CITY MANAGER'S COMMENTS

The City Manager RECOMMENDS approval of the foregoing.

COUNCIL POLICY

It is Council policy to fund capital expenditures for the waterworks, sewerage & drainage, and energy utility systems from debenture borrowing, and to fund the balance of capital expenditures from a combination of debenture borrowing, contributions from the Operating Budget ("Capital from Revenue"), Development Cost Levies, Community Amenity Contributions, and contributions from senior governments and third parties.

- Section 242 of the *Vancouver Charter* gives Council the authority to borrow funds for the construction, installation, maintenance, replacement, repair, and regulation of waterworks, sewerage and drainage, and energy utility systems without the assent of the electors.
- Section 245 of the *Vancouver Charter* requires that the borrowing authority for all other purposes be established through the approval of the electorate to specific borrowing questions associated with the City's capital planning process.

The requirement to borrow funds to finance capital expenditures is established by Council at the time of the approval of the annual Capital Budgets and through special approvals.

Borrowed funds are generally paid back over 10 years to ensure that a systematic borrowing program can be administered, that outstanding debt does not accumulate to unacceptable levels, and that interest costs are maintained at a level that does not put undue pressure on the operating budget.

- Section 247 A of the *Vancouver Charter* requires that full provision of annual debt charges, both principle and interest, be made in the annual operating budget. This ensures that debenture holders are paid the interest component at the prescribed rate and time, and that sufficient funding is available to retire the obligation at maturity.

As a pre-condition to an external debenture issue, Council authorizes the Director of Finance to set the rate, price and other terms and conditions on which the debentures will be issued, including the power to instruct the City's Fiscal Agent to proceed with the issue. In doing so, Council commits itself to follow through with the debenture issue and to pass the appropriate borrowing by-law after the debentures are sold.

PURPOSE

The purpose of this report is to seek Council's authorization for the Director of Finance to issue City of Vancouver debentures to finance the City's capital expenditure program.

The borrowing authorities as outlined in this report were established from the 2006-2008 and 2009-2011 Capital Plans through Council and electorate approval, and the requirement for debenture funding was approved by Council as part of the 2008 and 2009 Capital Budgets. Funding for the debt charges following from the proposed borrowing is provided in the 2010 Operating and Utility Budgets. In this final step in the process, the Director of Finance is seeking authority to exercise these authorities to finance the capital expenditure program.

BACKGROUND

In 1970, the City opted to maintain its own borrowing program outside of the newly created Municipal Finance Authority of British Columbia (the "MFABC"). In making that decision, Council noted a number of issues as follows:

- Lack of direct City representation on the MFABC
- Loss of autonomy over the timing, amounts, and terms and conditions of the debenture issues
- The requirement for City contribution to a debt repayment reserve at the MFABC
- Loss of autonomy over management of the sinking funds accumulated against City of Vancouver debentures

Since 1970, the City has continued to borrow in its own name and manage its debenture portfolio with full autonomy over the borrowing process pursuant to Council's authority as stipulated in the *Vancouver Charter*. During the same period, the City has maintained a credit rating that is generally equivalent to the MFABC. Currently, the City carries credit ratings from Moody's (AAA (negative)) and Standard & Poor's (AA (stable)). The City's credit ratings continue to be among the best municipal ratings in the country and are equivalent to the ratings of many Canadian regional municipalities, making City of Vancouver debentures an attractive investment in both the domestic market and other markets abroad. With respect to market access, the City has enjoyed the same level as the MFABC with no significant impact arising from the credit rating changes.

Given the City's record of strong financial position, the timing for a debenture issue is most often influenced by market conditions such as investors' appetite for a debenture issue and prevailing interest rates. The City completed its last issue in June 2009 with \$125 million in sinking fund debentures, maturing on December 2, 2019, sold in the Canadian market. The "all-in" cost was 4.991%, which was among the lowest on debt currently held by the City.

The City utilizes a Fiscal Agent to provide advice on the City's debenture issues and to lead a syndicate of investment brokers who purchase the City debentures and market them to investors all over the world. The current syndicate is co-led by RBC Global Markets and CIBC World Markets, two of the largest public sector debenture management firms in Canada.

DISCUSSION

Market Conditions

Staff have been monitoring the capital markets in the past few months. Since the June 2009 issue, interest rates continue to stay at a historically low level, and investors' appetite for

municipal debentures with good credit quality remains strong. These conditions suggest that the timing is right for a debenture issue in the next few weeks. At current rates, the "all-in" costs for an issue at this time would likely be approximately 4.5%, which is among the lowest for the City's debenture program since 1970. To take advantage of these conditions, the Director of Finance recommends that the City be positioned to proceed to market a \$140 million debenture issue and have the necessary approvals in place.

The City will have two options for a debenture issue: The December 2, 2019 issue, launched in June 2009, can be reopened or an entirely new issue can be launched, the choice being subject to market conditions. Re-opening an issue increases the amount of the debentures outstanding and enhances liquidity in the market which may have additional appeal to institutional investors. A new issue provides added flexibility on term and pricing.

As part of the City's cash management strategy, any debenture proceeds that are not immediately required to fund capital expenditures will be invested on an interim basis to reduce the costs. On the other hand, should market conditions change drastically that preclude such a launch, the capital expenditure program can also be financed internally while awaiting the next opportunity.

Debenture Issue Process

Given the market volatility and dynamics, the borrower needs to have flexibility to decide on the timing, structure, interest, and pricing of the issue, as well as the market to which the issue will be offered right up to the market launch. The schedule of Council meetings at which approval for debenture issues can be sought does not support such degree of flexibility. It has been Council practice to delegate the authority to initiate a debenture issue to the Director of Finance, in consultation with an advisory group consisting of the Mayor, the Chair of the City Services & Budgets Committee, and the City Manager. This group is empowered to make the final decision leading to the issuance of the debentures. Once this group approves the sale, Council is committed to pass the appropriate by-law as part of the debenture documentation package. This arrangement has worked well in the past and is recommended for the upcoming issue.

Fiscal Agent

As a periodic participant in the capital markets, the City relies on its Fiscal Agent to provide expert advice on market conditions; timing, size and structure of the issue; orderly marketing procedures to avoid conflicts with competing borrowers; and marketing strategy to achieve the lowest possible borrowing costs for the City. When the City is ready to launch an issue, the Fiscal Agent is responsible for managing the sale of the debentures through a syndicate of brokers.

As mentioned earlier, the City's syndicate is co-led by RBC Capital Markets and CIBC World Markets such that the role of the Fiscal Agent will alternate between the two firms. As CIBC World Markets led the last issue, RBC Capital Markets will act as the Fiscal Agent for the upcoming debenture issue contemplated in this report.

Borrowing Authorities

The \$140 million debenture issue contemplated in this report will be comprised of the following borrowing authorities:

	2006-2008 Capital Plan	2009-2011 Capital Plan	Total
Waterworks	\$ 17,827,000	\$ 3,773,000	\$ 21,600,000
Sewers & Drainage	\$ 21,630,000	\$ 3,370,000	\$ 25,000,000
Neighborhood Energy Utility	\$ 15,000,000		\$ 15,000,000
Public Works	\$ 13,400,000	\$ 19,875,000	\$ 33,275,000
Parks & Recreation	\$ 6,770,000	\$ 18,230,000	\$ 25,000,000
Community Legacy Projects	\$ 1,125,000		\$ 1,125,000
Public Safety & Civic Facilities	\$ 3,250,100	\$ 15,749,900	\$ 19,000,000
Total	\$ 79,002,100	\$ 60,997,900	\$140,000,000

The borrowing authorities for Waterworks and Sewer & Drainage have been approved by Council as part of the 2008 and 2009 Capital Budgets. The borrowing authority for the Neighborhood Energy Utility was approved by Council on July 9, 2008 (RTS# 7294) and March 5, 2009 (RTS# 7292). *(See below for further details on the NEU financing strategy.)* The balance of the issue is derived from borrowing authorities approved by the electorate for Public Works, Parks & Recreation, Community Legacy Projects, Public Safety, and Civic Facilities. Council approval for these program and project expenditures has been provided as part of the 2008 and 2009 Capital Budgets.

The construction budget for the Neighbourhood Energy Utility (“NEU”) was approved by Council in 2006 and 2008 and is currently \$29.3 million. Interim financing arrangements were approved subject to the system becoming operational. It is now appropriate to approve more permanent financing arrangements and retire the interim financing as follows:

- \$5 million low-interest loan from the Federation of Canadian Municipalities Green Municipal Fund available to the City one year after commencement of the NEU commercial operations (RTS# 7247)
- \$8.5 million grant from the Union of BC Municipalities Innovation Fund
- Approximately \$16 million in debenture financing after the NEU is operational.

Council is requested to approve borrowing authority of \$15 million at this time.

FINANCIAL IMPLICATIONS

The annual debt charges (principle and interest) on a \$140 million debenture issue are estimated at \$17.5 million. Funding required for 2010 (one coupon payment of \$3.2 million) has been provided for in the 2010 Operating Budget and Utility Budgets. Ongoing debt charges will be offset by the anticipated debt maturities and/or the use of debt charges stabilization reserves.

CONCLUSION

The Director of Finance recommends that Council authorize a City of Vancouver debenture issue of up to \$140 million to finance the City's capital expenditure program to take advantage of the market conditions.

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