



## ADMINISTRATIVE REPORT

Report Date: September 28, 2011  
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Meeting Date: October 4, 2011

TO: Vancouver City Council  
FROM: Director of Finance  
SUBJECT: Debenture Program - 2011

### RECOMMENDATION

A. THAT Council authorize the issuance of up to \$140 million City of Vancouver debentures, utilizing borrowing authorities approved as part of the 2009 and 2010 Capital Budgets and through special approvals (\$125 million) and unexercised borrowing authorities related to the energy neighborhood utility system (\$15 million) as follows:

• Waterworks	\$ 22,000,000
• Sewers & Drainage	\$ 32,000,000
• Public Works	\$ 15,000,000
• Parks & Recreation	\$ 25,000,000
• Public Safety & Civic Facilities	<u>\$ 31,000,000</u>
	\$ 125,000,000
• Neighborhood Energy Utility System	\$ 15,000,000
	<u>\$ 140,000,000</u>

B. THAT, until the borrowing authorities established pursuant to Recommendation A are 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 interest 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 has been 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, direct contribution from the annual Operating Budget (Capital from Revenue), Development Cost Levies and Community Amenity Contributions from developers, special-purpose reserves, internal loans, fees and levies collected from property owners, and contributions from senior governments and other funding partners.

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 & drainage and energy utility systems without the assent of the electorate. Section 245 requires that the borrowing authority for all other purposes be established through the electorate's approval of a borrowing plebiscite.

The requirement to borrow funds to finance capital expenditures is established by Council at the time of the approval of the annual capital budget 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 annual debt servicing charges (principal and interest) 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 servicing charges (principal 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 interest 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 enact 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 up to \$140 million City of Vancouver debentures to finance the City's capital expenditure program.

The borrowing authorities as outlined in this report include \$125 million established from the 2009-2011 Capital Plan through Council and electorate approval and the requirement for debenture funding approved by Council as part of the 2009 and 2010 Capital Budgets; as well as \$15 million unexercised borrowing authorities related to the neighborhood energy utility system. Funding for the debt servicing charges (principal and interest) arising from the proposed borrowing is provided in the 2011 Operating and Utility Budgets. As the final step in

the process, the Director of Finance is seeking authority to exercise these authorities to finance the capital expenditure program.

## BACKGROUND

The City is the only municipality in British Columbia that manages its own borrowing program outside of the Municipal Finance Authority of British Columbia (MFABC). Pursuant to Council's authority as stipulated in the *Vancouver Charter*, the City borrows in its own name and manages its debenture portfolio with full autonomy over the timing, amounts, and terms and conditions of the debenture issues, and management of the sinking funds accumulated against City of Vancouver debentures.

The City's credit ratings continue to be among the best municipal ratings in Canada - AAA (stable) by Moody's, AA (stable) by Standard & Poor's and DBRS - and are equivalent to the ratings of many Canadian regional municipalities, making City of Vancouver debentures an attractive investment in both domestic and international market. With respect to market access, the City has enjoyed the same level as the MFABC with no material difference in pricing.

Given the City's record of strong financial and liquidity position, the timing for debenture issuance is most often driven by capital market conditions such as global risk appetite, interest rates, and investors' demand. In recent years, the City has been accessing the market every 12 to 18 months, with the last domestic issue completed in March 2010: \$125 million 10-year sinking fund debentures, maturing on June 1, 2020, at an "all-in" cost of 4.623%.

The City utilizes a Fiscal Agent to provide expert advice on debenture issues and to lead a syndicate of investment brokers who purchase the City of Vancouver debentures and market them to domestic and international investors. 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 market in the past few months. As the global economy continues to slow down and the European sovereign crisis remains unresolved, interest rates have trended down significantly in recent months, approaching a historically low level. Despite market volatility, investors' appetite for municipal debentures with good credit quality remains strong. At current rates, the "all-in" cost for an issue at this time is estimated to be around 3.5%, 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 approval in place.

Integral to 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 debt carrying 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 Issuance Process

Given the market volatility and dynamics, the issuer needs to have a high degree of flexibility in determining the timing, structure, interest rate and pricing of the debenture issue right up to the market launch. The schedule of Council meetings at which approval for a debenture issue 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 enact the appropriate borrowing 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 market, 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 issuers; and marketing strategy to achieve the lowest possible borrowing cost 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 investment 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 RBC Capital Markets led the last issue, CIBC World Markets will act as the Fiscal Agent for the upcoming debenture issue contemplated in this report.

Integral to the financial stewardship and continuous process enhancement, staff will conduct a review of the syndicate structure and, where necessary, make appropriate recommendations in the next couple of months.

Borrowing Authorities

The \$140 million debenture issue contemplated in this report is comprised of borrowing authorities approved as part of the 2009 and 2010 Capital Budgets and through special approvals (\$125 million), and unexercised borrowing authorities related to the neighborhood energy utility system (\$15 million) as follows:

Waterworks	\$	22,000,000
Sewers & Drainage	\$	32,000,000
Public Works	\$	15,000,000
Parks & Recreation	\$	25,000,000
Public Safety & Civic Facilities	\$	<u>31,000,000</u>
	\$	125,000,000
Neighborhood Energy Utility System	\$	<u>15,000,000</u>
	\$	<u>140,000,000</u>

The borrowing authorities for Waterworks and Sewer & Drainage were established by Council and the borrowing authorities for Public works, Parks & Recreation, and Public Safety & Civic Facilities were established by the electorate as part of the 2009-2011 Capital Plan. The requirement to borrow funds to finance these capital expenditures was established by Council at the time of the approval of the 2009 and 2010 Capital Budgets and through special approvals. The remainder represents unexercised borrowing authorities related to the Neighborhood Energy Utility System from the 2006-2008 Capital Plan.

#### **FINANCIAL IMPLICATIONS**

The annual debt charges (principal and interest) on a \$140 million debenture issue are estimated at \$17.5 million. Funding required for 2011 (one interest payment of up to \$0.8 million) has been provided for in the 2011 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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