



REPORT

Report Date: June 23, 2020
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Meeting Date: July 21, 2020

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TO: Vancouver City Council
FROM: Director of Finance
SUBJECT: Debenture Program 2020

RECOMMENDATION

- A. THAT Council authorize the issuance of up to \$100 million of City of Vancouver debentures, utilizing borrowing authorities approved as part of the 2017, 2018 and 2019 Capital Budgets as follows:

Borrowing authorities from the 2015 -2018 Capital Plan:

Parks	\$	2,441,000
Recreation and Exhibition Facilities	\$	6,287,406
Public Safety Facilities	\$	2,829,225
Streets and Bridge Infrastructure	\$	7,000,996
Street Lighting, Traffic Signals and Communication Systems	\$	2,809,402
Community Facilities	\$	5,774,850
Civic Facilities and Infrastructure	\$	<u>2,885,020</u>
Subtotal 2015-2018 Capital Plan	\$	30,027,899

Borrowing authorities from the 2019 -2022 Capital Plan:

Sewers	\$	38,500,000
Street and bridge infrastructure	\$	15,000,000
Street lighting, traffic signals & communications systems	\$	5,000,000
Technology renewal projects	\$	2,500,000
Maintenance of community and civic facilities	\$	4,000,000
Renovations of community and civic facilities	\$	2,972,101
Maintenance and renovations of parks	\$	<u>2,000,000</u>
Subtotal 2019-2022 Capital Plan	\$	69,972,101

Total \$ 100,000,000

- 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 Finance and Services Committee, and the City Manager, or a majority of them, be empowered to act and instruct the City's bank syndicate 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 bank syndicate 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.

REPORT SUMMARY

The purpose of this report is to seek Council's authorization for the Director of Finance to issue up to \$100,000,000 of City of Vancouver debentures as part of its regular debenture funding program to finance the City's capital programs.

The borrowing authorities as outlined in this report were established in the 2015-2018 Capital Plan and the 2019-2022 Capital Plan through Council and electorate approval, and the requirement for debenture funding approved by Council as part of the 2017, 2018 and 2019 Capital Budgets. As the final step in the process, the Director of Finance is seeking authority to exercise these authorities to finance the capital programs.

Funding for the debt servicing charges (principal and interest) arising from the proposed borrowing will be provided in the annual Operating Budgets.

COUNCIL AUTHORITY/PREVIOUS DECISIONS

The City funds capital investments from a range of sources (who pays) using a balanced mix of payment methods (when to pay).

Funding Sources (Who Pays)

- **Property tax and user fees** to fund capital renewal work
- **Development contributions** (Development Cost Levies, Community Amenity Contributions, Density Bonus contributions, etc.) to fund growth-related amenities and infrastructure
- **Partner contributions** from senior levels of government, BC Housing, TransLink, foundations and philanthropists

Payment Methods (When to Pay)

- **Pay in advance** – set aside funds in reserves ahead of future capital investments
- **Pay-as-you-go** – allocate current revenues to fund ongoing capital programs
- **Pay over time** – finance large-scale capital investments that are cost-prohibitive to be funded on a pay-as-you-go basis, and enable taxpayers that benefit from the capital investments to share the costs over time

The City determines its long-term borrowing capacity by limiting the ratio of annual debt servicing to operating revenue at a maximum of 10%. This is to ensure that the City does not accumulate debt at unacceptable levels, and that annual debt servicing does not put undue

pressure on the annual budget. As part of the City's long-term debt management strategy, the water utility has transitioned its infrastructure lifecycle replacement program from debt financing to pay-as-you-go. A similar strategy is being undertaken with the Sewer utility. This will help lower the City's overall debt and save interest costs over the long term, and create room in its debt capacity to accelerate the asset renewal program in future years. Looking ahead, the City will continue to explore opportunities, where appropriate, to transition the general capital programs to a higher proportion of pay-as-you-go to improve the City's long-term debt profile and maintain its high quality credit ratings. The City will continue to monitor and adjust its financial strategy to strike a balance between debt financing and pay-as-you-go.

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 programs is established by Council at the time of the approval of the annual capital budget. 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 247A 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 appoint and instruct the City's bank syndicate 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 to investors.

CITY MANAGER'S/GENERAL MANAGER'S COMMENTS

The City Manager recommends approval of the foregoing.

REPORT

Background/Context

The City is the only local 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 of issuances, amounts, 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 with Aaa (stable) by Moody's Investors Service and AAA (stable) by S&P Global Ratings, making City of Vancouver debentures an attractive investment in both domestic and international markets. 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 rate environments, and investors' demand. The City has been accessing the market annually, with the recent re-opening of the existing 3.70% October 2052 sinking fund debenture in October 2019 to issue \$100 million at an "all-in" cost of 2.618%.

The City utilizes a bank syndicate of investment brokers to provide expert advice on debenture issues and to purchase City of Vancouver debentures and market them to domestic and international investors. The bank syndicate comprises of Bank of Montreal, Canadian Imperial Bank of Commerce, National Bank Financial, Royal Bank of Canada, Scotia Capital, TD Bank, Casgrain & Company Limited, and Canaccord Genuity, which collectively provides the widest debenture issuance coverage of investors for Canadian public sector issuers.

Strategic Analysis

Market Conditions

After the fall-out of COVID-19 lock down and the measures undertaken by the Bank of Canada to cut interest rates to near-zero, global economic activity showed unprecedented levels of intense market volatility. Despite this increased market volatility, investors' appetite for municipal debentures with good credit quality remains strong.

Recently, the estimated "all-in" cost for a 10-year issue is in the range of 1.50% to 2.00%, which would continue to be low by historical standards. The City has typically issued 10-year debentures, with the exception of a 40-year debenture issued in 2012 and the re-opening of this same 40-year debenture in 2019, to take advantage of the low interest rate environment. Staff will continue to monitor the market situation to determine an opportune time to issue. Depending on market conditions, the issuance may take place during the fall of 2020 or into the first half of 2021. The Director of Finance recommends that the City be positioned to proceed to market up to a \$100 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 programs 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 program can also be financed internally while awaiting the next opportunity.

Debenture Issuance Process

Given the market volatility and dynamics, the City 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 Finance and Services 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.

Bank syndicate

As a periodic participant in the capital market, the City relies on its bank syndicate to provide expert advice on market conditions; timing of issuances, 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 City’s bank syndicate is collectively responsible for managing the sale of the debentures. A senior lead from the bank syndicate will be chosen by the City to lead manage the debenture issuance.

Borrowing Authorities

The \$100 million debenture issue contemplated in this report is comprised of the following borrowing authorities established from the 2015-2018 and 2019-2022 Capital Plans:

<u>Borrowing authorities from the 2015 -2018 Capital Plan:</u>	
Parks	\$ 2,441,000
Recreation and Exhibition Facilities	\$ 6,287,406
Public Safety Facilities	\$ 2,829,225
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Subtotal 2019-2022 Capital Plan	\$ 69,972,101
Total	<u>\$ 100,000,000</u>

The requirement to borrow funds to finance these capital programs was established by Council at the time of the approval of the 2017, 2018 and 2019 Capital Budgets.

Debenture Structure

The City has been a regular annual debenture issuer in recent years. As reported in the 2019 Annual Financial report, the City had \$1,081.1 million in external long-term debt outstanding as of December 31, 2019. The City has accumulated \$476.4 million in Sinking Fund reserves for

retirement of this debt which leaves a net external debt outstanding of \$604.7 million. The summary of outstanding debt is included in Appendix A.

Financial Implications

The annual debt servicing charges (principal and interest) on a \$100 million debenture issue are estimated at approximately \$13 million, subject to bond market conditions upon issuance. Funding will be provided in the annual operating budgets. On-going debt charges will be offset by anticipated debt maturities and/or use of debt stabilization reserves.

CONCLUSION

The Director of Finance recommends that the City be positioned to proceed to market up to a \$100 million debenture issue and have the necessary approval in place.

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APPENDIX A
City of Vancouver Debenture Structure
As at December 31, 2019

Bylaw	Issued (\$ 000's)	Maturity	Interest rate
10015 ¹	125,000	2020-06-20	4.50%
10393	140,000	2021-12-02	3.45%
10565	120,000	2052-10-18	3.70%
10797	110,000	2023-10-24	3.75%
11080	105,000	2024-10-16	3.05%
11362	90,000	2025-11-20	2.90%
11673	90,000	2026-12-15	2.70%
11941	85,000	2027-11-03	2.85%
12203	85,000	2028-09-21	3.10%
12561	100,000	2052-10-18	3.70%
10117	2,959	2030-09-30	1.71%
12307	4,500	2028-11-20	4.07%
Total debentures	1,057,459		
Unamortized premium ²	23,644		
Gross debt	1,081,103		
Less: sinking fund reserves	(476,419)		
Net debt outstanding	604,684		

Notes to table:

1 – This debenture matured on June 20, 2020 as was repaid from sinking fund reserves.

2 – The unamortized premium relates to the accounting treatment for re-opening of the 2052 debentures.