City of Kingston
Information Report to Council
Report Number 19-254

To:	**Mayor and Members of Council**
From:	**Desirée Kennedy, Chief Financial Officer and City Treasurer**
Resource Staff:	**Lana Foulds, Director of Financial Services**
Date of Meeting:	**November 19, 2019**
Subject:	**Debt Management Plan**

Executive Summary:

At the July 9, 2019 meeting of Council, the following Council motion directed staff to provide information on the City of Kingston's ("the City") debt management plan and related capital funding strategies.

Whereas a core principle of Council's Strategic Plan, 2019-2022 is fiscal responsibility; and

Whereas the Corporation of the City of Kingston is in the range of $400,000,000 of debt, including debt issued on behalf of Utilities Kingston; and

Whereas the City of Kingston spends approximately $16,000,000 a year paying interest on this debt; and

Whereas the City of Kingston occasionally has unplanned surpluses from spending less than anticipated or receiving additional transfers from Utilities Kingston; and

Whereas said municipal surpluses are deposited into the working fund reserve of the City of Kingston to be spent on other projects and programs; and

Whereas reducing debt provides a return on investment in the form of savings on interest payments;

Therefore Be It Resolved That council direct staff to report back with detailed information on the City's debt management plan including but not limited to; long-term borrowing strategies, current and projected debt position, debt servicing costs and maturities as well as other measures and strategies that would reduce the City's reliance on debt by Q3 in time for the budgetary planning process of 2019-2020.

This report provides a summary of the City's debt management policies and practices since amalgamation and provides information on how debt levels and related servicing costs are managed.

A comprehensive long term fiscal plan and capitalization policy was approved by Council shortly after amalgamation which supported a commitment to increase capital investment and to build sustainable capital reserve fund balances. A dedicated one percent incremental capital levy and the responsible use of debt in the short term were approved strategies that were implemented in support of the long term fiscal plan.

Debt management strategies have been modified over time to accommodate financial requirements. With the implementation and continuation of the 1% capital levy the reliance on debt has lessened and outstanding debt balances are projected to decline. Paying for goods and services as resources will allow is the preferred funding option for asset replacement and renewal expenditures with debt funding used primarily for large scale projects and growth related investments.

The City of Kingston's 2018 Audited Financial Statements report a balance of $360M in issued debt. An additional $190M of debt approved but not yet issued is projected to be issued over the next three to four years as large scale projects are completed. Total debt outstanding is well below the provincial thresholds and is managed within the City's self-imposed limits. Sound management practices have also assisted the City to secure a continued 'AA' credit rating from Standard and Poor's. The City's draft 2020 capital budget recommendations do not contemplate adding any new debt over this term of Council.

Recommendation:

This report is for information only.

Authorizing Signatures:

ORIGINAL SIGNED BY CHIEF FINANCIAL OFFICER
AND CITY TREASURER

Desirée Kennedy, Chief Financial Officer and City Treasurer

ORIGINAL SIGNED BY CHIEF ADMINISTRATIVE OFFICER

Lanie Hurdle, Interim Chief Administrative Officer

Consultation with the following Members of the Corporate Management Team:

Peter Huigenbos, Acting Commissioner, Community Services	Not Required
Brad Joyce, Acting Commissioner, Corporate Services	Not Required
Jim Keech, President & CEO, Utilities Kingston	
Sheila Kidd, Commissioner, Transportation & Public Works	Not Required

Options/Discussion:

Introduction and Regulatory Framework

A fundamental component of capital planning is the ability of a municipality to incur long-term debt. Long-term debt is a capital financing tool that allows for the payment of capital assets over a period of time. Long-term debt is restricted for use in funding capital assets whose useful life and benefits extend over a number of years. As the benefits extend into the future, so can the payment for those benefits through an annual debt charge, supporting the principle that users are responsible for the costs of the benefits they receive. Capital funding strategies support two primary funding options – pay for goods and services as resources will allow (pay-as-you-go) or issue debentures and pay for them over time. Debentures are long-term loans, with a fixed payment schedule and rate of interest. Debenture terms can vary and are determined based many factors including the useful life of the asset, the value of the benefit that future generations will receive from the asset, other revenues that may be generated over time by the asset, cash flow projections to support repayments and current and projected interest rates.

It is important to note that in the municipal realm, long-term debt can only be used to fund capital projects. Unlike upper levels of government, municipalities cannot issue debt to fund operating deficits. If a municipality has an operating deficit in one year, they must raise taxes or other revenues in the following year to fund the prior year’s deficit.

Local governments generally cannot operate without incurring some debt for capital purposes. As an analogy, that would be the equivalent of all residents purchasing a home without the necessity for a mortgage. While the deferral of capital expenditures until funding resources are available is an option, reality is such that the need to support growth and to maintain the infrastructure necessary to support services will influence the timing of capital investments.

As part of Standard and Poor’s (S&P) annual credit rating review, they provided a comprehensive perspective with respect to the debt position of the Canadian municipal sector. It was noted that high levels of capital expenditures required to address growing infrastructure deficits, have contributed to a build-up of debt at the municipal level; however, from a credit rating perspective, the debt burden is still considered relatively low. Of the 35 rated entities, S&P noted that 30 have a credit rating of “AA” or higher. Strong operating performance in conjunction with a low debt burden underpin the credit quality of municipalities overall. Municipalities rely on a stable revenue source and growth prospects that are particularly relevant for the larger municipalities and low interest rates have helped municipalities to manage their cost of debt. Also noted, Canadian rated municipalities hold large liquidity reserves – on average rated Canadian municipalities have cash reserves worth 5.7 times their annual debt service which mitigates the risk of default. The City of Kingston currently has cash reserves worth approximately 4.3 times our annual debt service costs.

The regulatory framework governing municipal borrowing supports responsible debt management. The Province provides for municipalities to incur debt for municipal purposes in the *Municipal Act, 2001* with imposed limits in the form of a financial indicator that measures the proportion of current fund expenditures required for debt charges. This measure is similar to the one used by the banks in calculating the percentage of a household income that would be required to cover mortgage payments. *Ontario Regulation 403/02 Debt and Financial Obligation Limits* incorporates a limit on the amount of debt that a municipality may incur. That limit is calculated based on the overall guideline that no more than 25% of annual operating revenues (excluding certain revenues such as government grants and transfers from reserves and reserve funds) can be used for the payment of both interest charges and principal repayments.

The City Treasurer is required to report annually to Council on the municipality's debt limits, based on the latest Annual Repayment Limit (ARL) provided by the Ministry of Municipal Affairs. This report provides Council with information with respect to the municipality's existing levels of long-term debt as well as the additional long term borrowings that could be available as per the provincial guidelines. The 2019 Municipal Debt Limits report was provided to Council on April 16, 2019.

When a municipality proposes to undertake long-term borrowing (or other long-term financial obligations), the City Treasurer is responsible for updating the limit issued by the Province and for determining whether there is capacity for the proposed additional annual debt carrying costs within the municipality's ARL to undertake the planned borrowing.

Debt Policy

The City's current debt policy provides for the issuance of long-term debt at a level that will not impair the financial position of the municipality. It outlines principles that ensure debt is managed responsibly, in accordance with corporate goals, financial planning objectives and legislative provisions.

Inherent in the policy is the overriding philosophy that debt be affordable and financially sustainable. It establishes sustainable debt limits within legislative and internally imposed limits, ensures that debt is used strategically to fund capital projects and ensures that the debt is appropriately structured with sufficient revenues to cover annual debt servicing costs.

Specifically noted in the City's debt policy, the term of debt shall not extend beyond the useful life of the related asset with consideration for current interest rates, the value of the asset to future generations and revenue streams the asset may generate. The policy also directs that debt financing only be considered if other effective sources of financing are not available and that the municipality's annual debt limit not exceed 10% of previous year's own source revenues.

When Does Debt Make Sense?

There are differing philosophies over whether to use a “pay-as-you-go” approach (funding capital from existing capital reserve funds) versus “pay-as-you-use” (issuing debt and paying off the debt over the respective life of the capital asset). Depending on the municipality's size, service responsibility and fiscal policies, municipalities may decide to use long-term debt as a funding alternative to finance infrastructure and other capital assets. There are a variety of considerations discussed below that can influence a capital financing decision.

Affordability

Affordability and cash flow considerations may influence the decision to use debt financing. While the use of debt funding increases the total cost of a project by the additional cost of interest, it may also allow you to complete capital projects sooner.

Cashflow considerations

Municipalities may not have the resources to finance a capital project up front. Borrowing allows them to spread the cost of the project over its useful life and allows infrastructure costs to be paid by those benefiting from the service. Spreading payments over a longer period will also create a more predictable cash flow that aligns with annual revenue streams.

The benefit principle

Since current and future residents of the community will benefit from the capital assets, it is appropriate that both current and future residents should pay for the cost of that asset over its useful life.

The investment in capital assets supports the delivery of services to the community, often for many years. The decision to use debt financing for major capital expenditures spreads the cost of capital over the useful life of an asset in relation to the term of those benefits. Since current and future residents of the community will benefit from the capital asset, it is appropriate that both the current and future residents should pay for the cost of that asset over its useful life. Debt financing accomplishes this by charging project costs over a number of years in the form of debt servicing. As the benefits are being received, the cost of the capital asset supporting the service is being funded.

Low interest rates or escalating project costs

Interest rates are an important consideration for when and if to issue debentures. A low interest rate environment can be utilized to advance capital investment. If interest rates are lower than the rate of inflation for certain construction projects, it may make sense to borrow for a project sooner, rather than pay a higher cost for the project later.

Long-Term Fiscal Planning

On January 1, 1998, the City was amalgamated with Kingston Township and Pittsburgh Township to form the new City of Kingston. Post-amalgamation planning necessitated the municipality to consider its long term capital planning approach in an environment, not unlike many municipalities, that was dealing with aging infrastructure and an historic pattern of inadequate investment in capital assets. The approach required the development of a comprehensive long term fiscal plan and capitalization policy for the future of the newly amalgamated city. The following principles formed the foundation upon which the capital plan and related funding strategies would be developed:

- A commitment to address the increasing infrastructure deficit;
- A commitment to ongoing capital investment requirements to maintain, repair, and replace the City's existing capital asset portfolio;
- A commitment to the investment required for new capital to support the municipal and utility services needed for population growth;
- A desire to maintain responsible and consistent tax rate increases;
- A desire to maintain responsible debt levels; and
- A commitment to increase and maintain sustainable capital reserve fund balances.

More importantly, it was agreed that the primary objective of the long-term capital funding strategies over time would be an increased reliance on pay-as-you-go capital funding and reduced reliance on debt. This became the overarching principle that continues to influence our fiscal policy setting processes today.

In 1999, Council provided formal direction to develop a capitalization policy that reflected a progressive increase in contributions to capital reserve funds along with the responsible use of debt until such time as increased contributions would support a pay-as-you-go strategy.

The following motion was carried at the February 2, 1999 Council Meeting:

> **That**, subject to final budget review by Council, the following recommendations be approved:
>
> 1. That the municipality develop a Capitalization Policy that would include:
>   a) Progressive increase of contributions from current operation to reserves for Capital;
>   b) Initial increase of debt level, using debt capacity, until offset by pay-as-you-go;
>   c) Use of Utility dividends and asset sales as contributions to reserves
> 2. Create a Working Fund Reserve for stabilization of taxes, i.e. ad hoc events, snow precipitation variance, new legislation, etc.
> 3. Approve in principle the proposed budget strategies presented.

To implement the recommendations, the City introduced a capital policy in 1999 that included a 1% incremental tax increase allocated annually to infrastructure renewal and capital works, currently referenced as the 1% capital levy. The policy also incorporated a 1% incremental increase on fees and charges revenues also to be allocated for capital purposes. The annual fees and charges by-law supports this policy and ensures that the proportion of user fees and taxation subsidy for services is maintained.

The City's long term fiscal management has continued to be guided by the following capital investment strategies:

- Upgrading and replacing aging infrastructure and historic pattern of inadequate investment in capital assets.
- A fiscal plan to "catch up" and maintain the necessary level of investment in capital while managing debt levels.
- Strategies to:
  - Increase reliance on pay-as-you-go strategy
  - Reduce reliance on debt
  - Increase contributions to capital reserve funds
  - Support responsible use of debt in the short term
  - Support appropriate use of debt in the long term

Over the last 20 years, the City has remained committed to the post-amalgamation capital planning strategies. The 1% incremental capital levy remains in place with the objective of reaching a defined level of sustainable capital investment.

Where Are We Today?

<u>Contributions to capital reserve funds</u>

In 2019, the annual 1% capital levy contributed approximately $38M to capital reserve funds for municipal purposes. An additional $20M is contributed annually to the capital reserve funds through services that are supported in whole or in part by an incremental 1% annual increase on user fees and charges. With additional contributions from federal gas tax grants, investment income and other sources, approximately $75M is contributed annually to capital reserve funds for municipal purposes, supporting the increased use of pay-as-you-go capital funding. With the continuation of the 1% incremental capital levy, annual transfers to capital reserve funds for municipal purposes are projected to reach approximately $100M by 2026.

This level of contribution continues to move closer to a sustainable level of annual capital investment, which based on the existing capital asset portfolio is currently estimated to be in the range of $115M as outlined below. Staff continue to develop and implement asset planning strategies and to align asset management plans with provincial legislation. The first requirement is to develop a plan for core infrastructure assets by July 1, 2021. All other assets will be incorporated into the plan by July 1, 2023. These efforts will provide better data to more accurately identify the necessary capital investment required to properly maintain and replace the City's capital assets.

	Estimated Annual Capital Investment
Road and related infrastructure	**$ 40M**
Equipment and fleet	**15M**
Facilities	**12M**
Parks	**8M**
Information technology	**5M**
Total capital investment	**$ 80M**
Debt charges (principal and interest)	**35M**
Total	**$ 115M**

The City's long-term capital planning approach is also utilized for water, wastewater and gas services. Budgets for municipal utility services are presented to Council for approval. Utility rates are set through the budget process to fund municipal utility operations and related capital investment. Taxation revenues are not used to support municipal utility operations. Utilities Kingston has increased its annual contribution to utility capital reserve funds through utility rates over the past few years in order to reduce the reliance on debt for ongoing asset management investment. Utility operating budgets currently contribute approximately $30M annually to the utility capital reserve funds, for capital investment in water, wastewater and gas services.

The City's Debt Position

Further information is provided below with respect to the City's debt models and projected debt balances over the next fifteen years. The information illustrates that, in accordance with the 1999 capitalization policy, debt capacity has been used to attain an increased level of capital investment. Debt balances are projected to increase over the next three to four years before starting to decline as we reach a point where we no longer require the use of debt capacity to supplement the pay-as-you-go funding approach.

A review of the debt funding approvals as recommended in more recent annual capital budgets illustrates a reduced reliance on debt funding. In the past, debt funding was used to finance not only growth related or large scale projects but also routine asset management costs to maintain and rehabilitate existing assets. As capital reserve funds have built up over time, the City has been able to increase its use of pay-as-you-go funding for asset replacement and renewal investments and limit debt funding for significant projects and growth related investments.

This has been evidenced by the last four years of annual capital budget submissions which recommended the strategic use of debt funding for the following major projects only: Kingston East Community Centre $7.0M; Central Library Renovations $11.3M; Airport Expansion $10.0M and K&P Trail $3.0.

The City of Kingston's Audited Financial Statements at December 31, 2018 reported a total long-term debt balance of $366.7M of which $360.3M relates to debt issued by the City. Of the total debt, 37% is tax supported, 25% is repaid through user charges and 38% is repaid through utility rates. Debenture terms generally align with the useful life of the respective capital asset; the City's outstanding debentures have varying maturities up to 2047. City of Kingston's total debt outstanding per capita is approximately $2,850 (tax and ratepayer supported).

	2018	2017
	(In thousands of dollars)	
Long-term liabilities incurred by the City, with varying maturities up to 2047 and a weighted average interest rate of 4.0%	$ 360,376	$ 375,759
Long-term liabilities incurred by Kingston & Frontenac Housing Corporation, with an interest rate of 5.4%, 3.6% and 3.0%, maturing 2028, 2032 and 2036	6,008	6,237
Long-term liabilities incurred by Town Homes Kingston, with interest rates ranging from 2.1% to 6.5% and varying maturities up to 2028	13,374	14,361
Proportionate share of KFLA Public Health long-term debt, with a current interest rate of 6.1%, maturing in 2029	3,061	3,270
Total long-term liabilities	$ 382,819	$ 399,627
Less long-term borrowings from own funds	(16,104)	(17,095)
Long-term liabilities to be recovered from future revenues	$ 366,715	$ 382,532

The outstanding debt balance includes debt issued for municipal as well as water and wastewater infrastructure. The following provides a breakdown of the City's outstanding debt balance of $360.3M by source of repayment.

Repayment source	Outstanding Debt at December 31, 2018 ($M)	Repayment Source (%)
Tax Supported	$ 132.0	37%
Utility Rates	137.4	38%
User Charges	90.9	25%
Total Debt Issued at December 31, 2018	$ 360.3	100%

The audited financial statements also provide information on the principal payments due on the total long-term liabilities by source of repayment as follows:

(In thousands of $)	2019	2020	2021	2022	2023	2024+	Total
Tax sources	$ 7,364	$ 7,612	$ 7,870	$ 8,082	$ 8,303	$ 92,826	$ 132,057
Utility user fees	4,620	4,773	4,935	5,103	5,278	112,685	137,394
Other user fees	2,643	2,769	2,902	3,040	3,188	76,383	90,925
Public Health	224	239	255	272	291	1,780	3,061
Town Homes	1,089	1,132	1,178	1,225	1,006	7,744	13,374
Housing Corp	239	250	262	275	288	4,694	6,008
	$ 16,179	$16,775	$17,402	$ 17,997	$18,354	$296,112	$ 382,819

Debt Approved and Not Yet Issued

At December 31, 2018, there was $193.6M of debt previously approved by Council but not yet issued. Several large projects make up the majority of the outstanding amount including:

Project	Balance Approved Not Yet Issued December 31, 2018 ($M)
Cataraqui Bay Wastewater Treatment Facility	$ 78.0
Third Crossing (Municipal and Development Charges)	30.0
John Counter Boulevard Widening	15.6
Central Library Renovations	12.1
Rideau Heights Community Centre	10.5
Airport Expansion	10.0
Fleet Maintenance Garage	9.5
Kingston East Community Centre	6.0
Other	21.9
Total Debt Approved Not Yet Issued December 31, 2018	$ 193.6

The balance of debt approved but not yet issued will be strategically issued over the next three or four years as projects are complete to ensure that total outstanding debt balances remain within a self-imposed maximum capacity level as discussed further below.

Debt Models

The City's financial capacity and financing models reflect the capital and financing requirements for capital asset reinvestment strategies as well as new capital asset investments as provided for in the 15 year capital plans. Debt models are updated annually to reflect the 15-year capital plans.

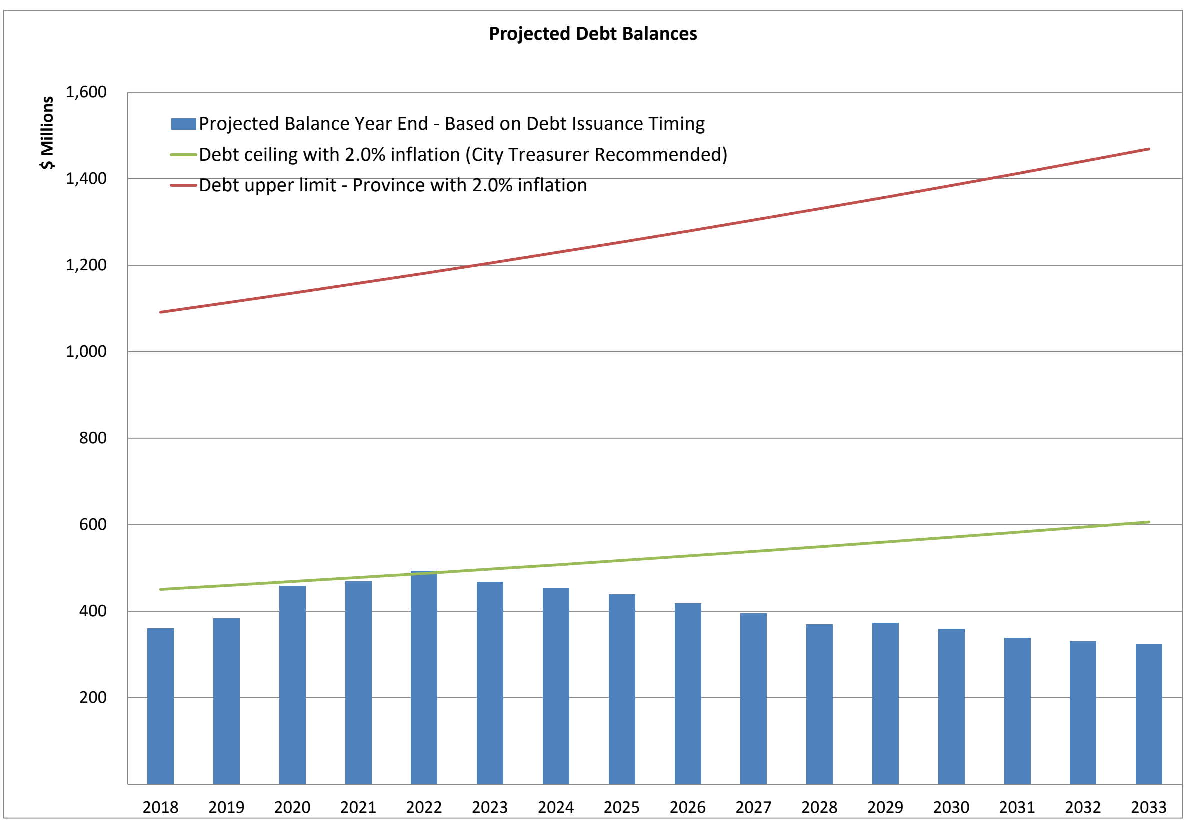
Capital expenditures are financed primarily through the City's capital reserve funds, using a pay-as-you-go method whereby funds are withdrawn from the reserve funds to pay for the capital costs or through the issuance of debt whereby funds are borrowed to pay for the capital costs and the capital reserve funds are utilized to pay debt principal and interest charges. The continuation of the 1% annual increase for capital infrastructure purposes, as endorsed by Council, is incorporated in the capital funding models until annual capital investments are at a sustainable level based on the existing capital asset portfolio at which time strategies for reducing the incremental levy can be considered.

The graph below illustrates the City's debt models. The vertical bars depict the level of debt over time based on the cash flow analysis of the approved and future planned debt financing for the capital expenditure requirements over the 15 year projection period. The graph includes a line that reflects the provincial ceiling indexed at the rate of 2% to which the City could borrow and still be within its provincial debt capacity level. However, Council has endorsed the City Treasurer's recommendation to remain substantially below the provincial ceiling using a self-imposed maximum capacity level in 2019 of $460M, escalated at 2% for future years in line with projected inflation. This self-imposed maximum considers cash flow requirements and reflects the City's ability to manage debt. Standard and Poor's rating methodology is also considered in order to maintain a preferred credit rating. Staff continue to update capital plans and reprioritize projects and scheduling in order to manage financial capacity and debt balances.

This graph depicts the estimated debt levels over the next 15 years based upon the 2019 capital budget forecasts. As discussed above, the graph shows that over time the reliance of debt will decrease for the municipality. It also demonstrates that debt levels are significantly lower than the restrictions imposed by the Provincial government.

The graph shows that the level of debt only marginally exceeds the desired levels in 2022; however, it is projected to correct itself and thereafter will be well below the parameter ceiling. Conservative assumptions have been used in projecting future debt and it is likely that the actual timing of projects will provide further opportunity to defer the timing of debt issuance in order to remain well below accepted levels.

The debt model illustrates, 20 years after the implementation of the City's capitalization policy in 1999, the success of Council's objectives. Not only has the City used debt capacity to increase the necessary level of capital investment, it is projecting reduced debt levels into the future in conjunction with an increased pay-as-you-go funding strategy. The graph illustrates that the responsible use of debt in the short term will be replaced with increased reliance on a pay-as-you-go strategy in the longer term.



Debt Servicing Costs

Debt financing of capital expenditures is repaid through annual debt charges for the term of the debenture. Debt servicing cost is the amount of principal and interest that a municipality must pay each year to repay the debt and related interest. The City's debt servicing costs are funded by capital reserve funds, using up some of the funding capacity available to fund pay-as-you-go capital expenditures. In 2018, the City paid approximately $30M in total debt charges including principal and interest payments, on both municipal and utility debt.

As discussed above, the Province imposes limits in the form of a financial indicator that measures the proportion of current fund expenditures required for debt charges, based on an acceptable percentage of operating revenues. That limit is calculated based on the overall guideline that no more than 25% of own source revenues (defined as annual operating revenues excluding certain revenues such as government grants and transfers from reserves and reserve funds).

The City's 2018 annual debt service costs as a proportion of own source revenues was 7.4%, well below the Provincial threshold of 25% of own source revenues. Own source revenues are made up of taxation revenues and revenues internally generated from programs and services; government grants and transfers from reserves and reserve funds are excluded from own source revenues. The City's debt policy currently provides for a maximum debt repayment limit of 10%.

Standard & Poor's Credit Rating

A credit rating is an unbiased, informed opinion about an issuer's likelihood to meet its financial obligations in full and on time. Credit ratings provide transparent third-party information that's not only forward-looking, but standardized for consistency. They serve as a universal benchmark to assess and demonstrate creditworthiness and while they are not a guarantee or absolute measure, they are a crucial tool for investors in the decision-making process.

Credit ratings are issued by an independent credit rating agency using a combination of qualitative and quantitative methods to determine the overall rating. Every year Standard and Poor's performs a comprehensive review of the City's financial records and policies. This review considers a broad range of factors in evaluating the creditworthiness of a municipality:

- Strength and stability of the economy – including development activity, demographic trends and assessment base
- Management and governance – including Council priorities, senior staff composition and financial policies
- Budgetary performance – including operating budgets and assumptions, capital expenditure and funding plans, tax and revenue capacity

- Debt balances – including debt issuance projections and long term debt forecasts
- Liquidity – including cash and investment balances

As a result of the rating review, Standard and Poor's releases a credit rating and outlook assessment. The following is an excerpt from Standard and Poor's rating definitions:

Rating	Definition
AAA	Investment Grade: Extremely strong capacity to meet financial commitments
AA	Investment Grade: Very strong capacity to meet financial commitments
A	Investment Grade: Strong capacity to meet financial commitments, but somewhat susceptible to economic conditions and changes in circumstances
BBB	Investment Grade: Adequate capacity to meet financial commitments, but more subject to adverse economic conditions
BB	Speculative Grade : Less vulnerable in the near-term but faces major ongoing uncertainties to adverse business, financial and economic conditions
B	Speculative Grade : More vulnerable to adverse business, financial and economic conditions but currently has the capacity to meet financial commitments
Below B	Speculative Grade : Various levels of vulnerability, dependent on economic conditions, default likely

Standard and Poor's recently released their 2019 Research Update Report which affirmed the City's 'AA' credit rating with a stable outlook. The report commented on the City's local economy – its positive demographic trends, the role tourism plays and the recently made gains in the food processing industry. It also gave credit to the City's financial management strategies, prudent debt and liquidity policies, manageable debt levels and a strong political consensus in setting strategic priorities and approving budgets that are built on realistic assumptions.

The credit rating process is an important validation of our fiscal strategies and approach. As discussed above, the City implemented a long term fiscal plan in 1999, using debt capacity to fund increased capital investment until such time as increased capital reserve fund contributions would support a pay-as-you-go strategy. It is important to note that the long-term fiscal plan was accompanied by a credit rating that continued to climb, confirming the rating agency's confidence in the City's long-term fiscal approach. The table below summarizes the annual credit ratings issued by S&P back to 2001. Exhibit 'A' provides further comparator analysis of municipal credit ratings. The Credit Rating Highlights document is regularly published by CIBC and provides a summary of current credit ratings for all three levels of government.

Year of review	Credit Rating	Year of review	Credit Rating
2019	AA / stable outlook	2009	No 2009 release, due to change timing of annual review
2018	AA / stable outlook	2008	A+ with a positive outlook
2017	AA / stable outlook	2007	Upgraded to A+ with a positive outlook
2016	AA / stable outlook	2006	A+ with a stable outlook
2015	AA / stable outlook	2005	A+ with a stable outlook
2014	AA / stable outlook	2004	A+ with a stable outlook
2013	AA / stable outlook	2003	A+ with a stable outlook
2012	Upgraded to AA / stable outlook	2002	A+ with a stable outlook
2011	Upgraded to AA-/positive outlook	2001	A with a stable outlook
2010	Upgraded to AA- / stable outlook		

Debt Reduction Strategies

The majority of the City's long term borrowing is done through Infrastructure Ontario, a Crown Agency of the Province of Ontario which supports the renewal of public sector infrastructure by delivering affordable long-term loans to municipalities and other public sector clients. Rates available through Infrastructure Ontario have generally been more competitive than local lending institutions or private debenture issues and the issuing process is streamlined and efficient. Rates are fixed for the term of the debenture providing stable cash flow requirements and eliminating the risk of volatility in interest rates.

<u>Prepayment of debt</u>

Prepayment of an issued debenture with Infrastructure Ontario is discouraged. Similar to other borrowing instruments, agreements with Infrastructure Ontario include penalty clauses for breaking any of the terms. Once the loan is locked in with Infrastructure Ontario, debentures are issued in the market and purchased by investors to match the length of the loan term. If the debenture was to be broken and the loan paid down, a breakage fee would be issued by the market as the debenture would have to be re-set/re-structured. The fee could be significant depending factors such as current market conditions, the loan amount, how many years are left in the term and the effective interest rate.

There are number of other debt reduction strategies that contribute to the management of debt funding levels.

Pay-as-you-go funding

Where possible, pay-as-you-go-funding is the preferred funding option for capital asset replacement and renewal investment. Where debt funding has been approved, subsequent changes in financial resources can provide an opportunity, as part of the capital project close out process, to switch out previously approved debt funding for funding from capital reserve funds. Funding changes would be recommended to Council for approval as part of the quarterly capital status reports.

Project prioritization

Capital plans are impacted by changing priorities, which can require Council and staff to reprioritize projects and scheduling in order to address related financial and resource capacity. Project prioritization considers debt funding requirements and can provide an opportunity to defer or reduce the need for debt.

Capital project surpluses

When a completed capital project has come in under budget, final funding reconciliations will, where possible, reduce debt funding rather than pay-as-you-go funding to recognize the surplus position. Funding changes would be recommended to Council for approval as part of the quarterly capital status reports.

Accelerated repayment terms

While debenture terms normally align with the useful life of an asset, considerations such as cash flow availability may provide opportunity to accelerate repayment terms.

Debt Funded Project Dashboard

The following table provides information at the project level of a sample of major capital projects with debt funding by year of issuance, details of debenture terms and outstanding debt balances at December 31, 2018. The information illustrates the drawdown of debt over time by project as well as the historical trend of interest rates.

While spending and close out details are provided at a project level when the project is complete and reported out to Council as part of the quarterly capital project status reports, debt is issued and managed at a consolidated level, with debentures often issued for a number of different projects.

For the sample of projects below, we have combined the project and debenture information. We have also referenced the respective capital project close out report which provides further detail on the project's total cost, budget variance and non-debt funding sources upon closing. For larger projects, staff will review opportunities to expand project information as part of the capital close out report to include a broader summary of the project details including budget to actual results, sources of funding and debenture terms, where applicable.

Project	Council Report Close Out	Approved Total Budget	Final Total Cost	Total Debt Issued	Debt Funding	Year of Issuance	Debt Term (Years)	Interest Rate	Debt Maturity	December 31, 2018 Outstanding External Debt
Point Pleasant Water Facility	N/A	62,190,788	62,075,495	11,800,000	Utilities	2017	30	3.41%	2047	11,569,117
				26,500,000	Impost	2017	30	3.41%	2047	25,981,491
Artillery Park	16-106	14,047,618	14,050,104	10,946,618	Municipal	2017	25	3.34%	2042	10,660,600
Calvin Park Library	10-307	5,300,000	5,303,862	3,000,000	Municipal	2012	25	3.79%	2037	2,220,000
Invista Centre	09-239	33,607,750	32,593,482	30,842,757	Municipal	2009	30	5.27%	2039	26,578,668
Grand Theatre	09-239	17,252,400	11,727,400	6,727,400	Municipal	2009	30	5.27%	2039	5,659,535
				5,000,000	Municipal	2005	25	4.96%	2030	3,180,119
Police Building	09-102	37,080,000	37,136,718	9,641,718	Municipal	2009	30	5.27%	2039	8,111,254
				8,350,000	Municipal	2008	10	2.11%	2018	-
				12,005,000	Municipal	2005	25	4.96%	2030	7,635,463
Leon's Centre	09-239	46,500,100	45,133,892	25,500,000	Municipal	2007	30	5.39%	2039	21,375,575
Market Square	09-239	6,185,000	6,117,949	845,000	Municipal	2005	25	5.03%	2030	537,440
				1,362,204	Municipal	2005	25	4.50%	2030	1,055,463
				500,000	Municipal	2005	10	4.50%	2015	-

Conclusion

Debt is one of the traditional funding sources accessed by municipalities to help finance the cost of municipal infrastructure. The City's capital investment and debt management strategies continue to reflect the philosophy of the corporation's long-term fiscal plan approved by Council in 1999. Increased reliance on pay-as-you-go funding and reduced reliance on debt will continue to support an increasing and sustainable level of capital investment with responsible use of debt capacity in the short-term and appropriate use of debt in the long term.

In accordance with debt policy, the following objectives will continue to influence the City's capital financing and debt program:

- Adhere to statutory requirements and self-imposed limits
- Maintain a strong credit rating
- Ensure long term financial flexibility
- Limit financial risk exposure
- Minimize long-term cost of financing
- Maintain appropriate balance of capital reserve funds

- Align the term of financing with the useful life of the capital asset or related term of benefit
- Be responsive and fair to both current and future taxpayers

The City's draft 2020 capital budget recommendations do not contemplate adding any new debt over the remaining term of Council. Over the same term, principal repayments of more than $15M will be made annually, reducing the total long-term debt balance by more than $60M.

The continuation of the long-term capital planning strategies as outlined in this report will require the ongoing commitment of Council to support the objectives listed above and to prioritize capital investment in a manner that will address financial and resource capacity.

Existing Policy/By-Law:

Capital Policy

Debt Policy

Tangible Capital Asset Policy

Capital budget by-laws for all years up to and including 2019 with capital budget amendments as approved by Council.

Notice Provisions:

Not applicable

Accessibility Considerations:

Exhibit A to this report will be provided in an alternate format upon request.

Financial Considerations:

Not applicable

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Exhibits Attached:

Exhibit A: CIBC Credit Rating Highlights

Canadian Government Credit Ratings

Macro Strategy

Government Credit

August 22, 2019

Credit Rating Highlights

Our latest summary of Canadian public sector credit ratings/outlooks follows. We highlight changes since our last update on June 19, 2019.

City of Edmonton's long-term debt was downgraded to AA Stable from AA+ Negative by S&P (July 25, 2019): "The downgrade reflects Edmonton's significant capital spending plans and corresponding growth in debt over the next several years. Under our new criteria, our assessment of a government's debt burden is weighted more heavily in its individual credit profile than before. However, this criteria change, by itself, was not the prominent factor in our decision to lower the ratings. Edmonton recently approved the C$2.6bln total cost and funding strategy for the Valley Line West light rail transit (LRT) project. We understand the provincial and federal governments have committed about C$2bln in grants to fund construction, allowing the city to build a key piece of infrastructure without placing excessive stress on its credit profile. Still, Edmonton's own funding contribution of about C$600mln is significant, in our view, particularly given that the city is also funding the final construction stages of the Valley Line Southeast LRT, in addition to several other notable projects. Taken together, we expect these projects to lead to wider after-capital deficits in 2019 and 2020, with the associated borrowing requirements keeping Edmonton's tax-supported debt burden more in line with that of 'AA'-rated peers."

Province of Newfoundland and Labrador and City of St. John's downgraded to A1 Stable from Aa3 Negative by Moody's (July 29, 2019): "The downgrade of the BCA to a3 and long-term debt ratings to A1 reflects Newfoundland and Labrador's elevated debt and interest burdens and continued expectation of material consolidated deficits over the next 2 years. The downgrade also reflects heightened credit risk stemming from the large debt level and weak financial metrics of Nalcor, the province's wholly owned utility, which raises the likelihood the province will need to provide financial support to, or assume debt service from, Nalcor." St. John's rating follows the province's: "Moody's notes that fiscal pressures faced by the province, reflected in the provincial rating action, are not expected to impact the standalone creditworthiness of the city, which is reflected by the affirmation of the a1 BCA. The A1 rating reflects Moody's baseline credit assessment (BCA) of a1 for the City of St. John's as well as the assumption of a high level of extraordinary support from the Province of Newfoundland and Labrador (A1 stable) should St. John's face an acute liquidity stress."

County of Lambton rating raised to AA Stable from AA- Stable on application of revised criteria by S&P (August 1, 2019): "The upgrade reflects our application of the new criteria, under which we assign a smaller weighting to Lambton's relatively limited budget flexibility than before. Lambton continues to benefit from a track record of healthy and stable budgetary balances and a very low debt burden, well below 30% of operating revenues. It also demonstrates sound financial management practices, which support strong budget results. At the same time, we expect the county's economic growth will remain slower than its peers."

Province of Prince Edward Island upgraded to A Stable from A(low) Positive by DBRS (August 15, 2019): "The upgrades recognize the sustained improvement in the Province's credit profile over the past five years. The Province has pursued pro-growth policies aimed at increasing the population, which have materially lifted economic activity and improved the longer-term economic outlook. The previous Liberal government undertook a significant multi-year effort to balance the provincial budget, and as a result, the Province has presented either balanced or positive operating results in each of the past three years. Improved operating results and stronger economic growth have contributed to reduced borrowing requirements and a pronounced decline in the Province's debt-to-gross domestic product (GDP) ratio."

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City of Yellowknife's outlook changed to Stable from Negative by Moody's (August 16, 2019): "The revised outlook to stable from negative reflects an improved forecast of financial metrics under the city's revised funding plan for key capital projects, resulting in lower debt accumulation than previously anticipated. Moody's now expects that Yellowknife's net debt will only rise modestly to around 60% of operating revenue by 2021 (from 50% in 2018) to finance the replacement of the city's aging water intake pipeline and its new aquatic center. Moody's revised expectations are primarily due to the city benefitting from federal funding support for the projects, including CAD25.8mln under the federal Disaster Mitigation and Adaptation Fund that is expected to cover 75% of the cost of the pipeline replacement."

Long-Term Credit Ratings

Issuer	DBRS	Fitch	Moody's	S&P
Sovereign				
Canada, Government of	AAA	AAA	Aaa	AAA
Federal Crown Corporations/Trusts				
Business Development Bank of Canada	AAA	–	Aaa	AAA
Canada Housing Trust No.1	AAA	–	Aaa	AAA
Canada Mortgage & Housing Corp.	AAA	–	Aaa	AAA
Canada Post Corp.	AAA	–	Aaa	–
Canadian Wheat Board, The	–	–	–	–
Export Development Canada	AAA	–	Aaa	AAA
Farm Credit Canada	AAA	–	Aaa	AAA
Muskrat Falls/Labrador Transmission Assets Fdg Trust/ Labrador Island Link Fdg Trust	AAA	–	Aaa	AAA
Strait Crossing Finance Inc.	–	–	Aaa	–
Other				
First Nations Finance Authority	–	–	A2	A+

Issuer	DBRS	Fitch	Moody's	S&P
Provincial and Provincially Guaranteed				
Alberta, Province of	AA [Neg]	AA	Aa1 [Neg]	A+
Alberta Treasury Branches (ATB Financial)	–	–	Aa1 [Neg]	–
Alberta Capital Finance Authority (ACFA)	AA [Neg]	–	Aa1 [Neg]	A+
British Columbia, Province of	AA(high)	AAA	Aaa	AAA
British Columbia Hydro & Power Authority	AA(high)	–	Aaa	AAA
Manitoba, Province of	A(high)	–	Aa2	A+
New Brunswick, Province of	A(high)	–	Aa2	A+
New Brunswick Municipal Finance Corp.	A(high)	–	Aa2	A+
Newfoundland & Labrador, Province of	A(low)	–	A1	A
Newfoundland & Labrador Hydro*	A(low)	–	–	A
Newfoundland & Labrador Municipal Financing Corp.	A(low)	–	–	–
Northwest Territories, Government of the	–	–	Aa1	–
Nova Scotia, Province of	A(high)	–	Aa2	AA-
Nova Scotia Municipal Finance Corp.	A(high)	–	–	–
Nunavut, Government of	AA(low)	--	--	--
Ontario, Province of	AA(low)	AA-	Aa3	A+
Ontario Electricity Financial Corp.	AA(low)	–	Aa3	A+
Prince Edward Island, Province of	A	–	Aa2	A
Québec, Province of	A(high) [Pos]	AA-	Aa2	AA-
Financement-Québec*	A(high) [Pos]	AA-	Aa2	AA-
Hydro-Québec*	A(high) [Pos]	AA-	Aa2	AA-
Saskatchewan, Province of	AA	AA	Aaa	AA
Yukon, Territory of	–	–	–	AA

*Guaranteed Long-Term Debt

Municipalities — Alberta				
Calgary, City of	AA(high)	–	–	AA+
Edmonton, City of	–	–	–	AA
Municipalities — British Columbia				
Municipal Finance Authority of British Columbia	–	AAA	Aaa	AAA
TransLink (South Coast British Columbia Transportation Authority)	AA	–	Aa2	–
Vancouver, City of	–	–	Aaa	AAA
Municipalities — Manitoba				
Winnipeg, City of	–	–	Aa2	AA
Municipalities — Newfoundland & Labrador				
St. John's, City of	–	–	A1	A+
Municipalities — Northwest Territories				
Yellowknife, City of	–	–	Aa2	–
Municipalities — Ontario				
Barrie, City of	–	–	–	AA
Belleville, City of	–	–	–	AA-
Brampton, City of	–	–	–	AAA
Durham, Regional Municipality of	–	–	Aaa	AAA
Essex, County of	–	–	–	AA+
Guelph, City of	–	–	–	AA+
Haldimand, County of	–	–	–	AA
Halton, Regional Municipality of	–	–	Aaa	AAA
Hamilton, City of	–	–	–	AA+

Issuer	DBRS	Fitch	Moody's	S&P
Municipalities — Ontario cont'd				
Kingston, City of	–	–	–	AA
Lambton, County of	–	–	–	AA
London, City of	–	–	Aaa	–
Mississauga, City of	–	–	–	AAA
Muskoka, District Municipality of	–	–	Aa2	–
Niagara, Regional Municipality of	–	–	–	AA
Norfolk, County of	–	–	–	AA-
North Bay, City of	–	–	Aa2	–
Ottawa, City of	–	–	Aaa	AA
Oxford, County of	–	–	–	AA+
Peel, Regional Municipality of	–	–	Aaa	AAA
Peterborough, City of	–	–	–	AA
Sault Ste. Marie, City of	–	–	–	AA-
Simcoe, County of	–	–	–	AA
Thunder Bay, City of	–	–	–	AA
Toronto, City of	AA	–	Aa1	AA
Waterloo, Regional Municipality of	–	–	Aaa	–
Wellington, County of	–	–	–	AA+
Windsor, City of	–	–	–	AA
York, Regional Municipality of	–	–	Aaa	AA+
School Boards/Infrastructure — Ontario				
55 School Board Trust, The	–	–	Aa3	A+
Durham District School Board	–	–	–	A+
Ontario Infrastructure and Lands Corp. (OILC)	–	–	Aa3	–
Ontario School Boards Financing Corp.	AA(low)	–	A1	–
Ottawa Catholic School Board	–	–	–	A+
Simcoe County District School Board	–	–	–	A+
Toronto Community Housing Corp.	–	–	–	AA-
York Region District School Board	–	–	–	A+
Municipalities — Québec				
Laval, Ville de	–	–	–	AA
Montréal, Ville de	A(high)	–	Aa2	AA-
Québec, Ville de	–	–	Aa2	–
Société de transport de Montréal	A(high)	–	Aa2	AA-
Municipalities — Saskatchewan				
Regina, City of	–	–	–	AAA
Saskatoon, City of	–	–	–	AAA

Source: CIBC Capital Markets - Macro Strategy, DBRS, Fitch, Moody's, S&P

Short-Term Credit Ratings

Issuer	DBRS	Fitch	Moody's	S&P
Sovereign				
Canada, Government of	R-1(high)	F1+	P-1	A-1+
Federal Crown Corporations/Trusts				
Business Development Bank of Canada	R-1(high)	–	P-1	A-1+
Canada Mortgage & Housing Corp.	R-1(high)	–	P-1	A-1+
Canada Post Corp.	–	–	P-1	–
Export Development Canada	R-1(high)	–	P-1	A-1+
Farm Credit Canada	R-1(high)	–	P-1	A-1+
Provincial and Provincially Guaranteed				
Alberta, Province of	R-1(high) [neg]	F1+	P-1	A-1+
Alberta Treasury Branches (ATB Financial)	–	–	P-1	–
British Columbia, Province of	R-1(high)	F1+	P-1	A-1+
British Columbia Hydro & Power Authority	R-1(high)	–	–	–
Manitoba, Province of	R-1(mid)	–	P-1	A-1
New Brunswick, Province of	R-1(mid)	–	–	A-1+
New Brunswick Municipal Finance Corp.	R-1(mid)	–	–	–
Newfoundland & Labrador, Province of	R-1(low)	–	–	A-1
Newfoundland & Labrador Hydro	R-1(low)	–	–	A-1
Nova Scotia, Province of	R-1(mid)	–	–	A-1+
Nova Scotia Municipal Finance Corp.	R-1(mid)	–	–	–
Ontario, Province of	R-1(mid)	F1+	P-1	A-1
Prince Edward Island, Province of	R-1(low)	–	–	A-1
Québec, Province of	R-1(mid)	F1+	P-1	A-1+
Financement-Québec	R-1(mid)	F1+	P-1	A-1+
Hydro-Québec	R-1(mid)	F1+	P-1	A-1+
Saskatchewan, Province of	R-1(high)	F1+	–	A-1+
Municipalities — Alberta				
Calgary, City of	R-1(high)	–	–	A-1+
Edmonton, City of	–	–	–	A-1+
Municipalities — British Columbia				
Municipal Finance Authority of British Columbia	–	–	P-1	A-1+
TransLink (South Coast British Columbia Transportation Authority)	R-1(mid)	–	–	–
Vancouver, City of	–	–	–	A-1+
Municipalities — Ontario				
Ottawa, City of	–	–	P-1	–
Toronto, City of	–	–	P-1	A-1+
Municipalities — Québec				
Montreal, Ville de	–	–	P-1	–
Société de transport de Montréal	R-1(low)	–	P-1	A-1+

Source: CIBC Capital Markets - Macro Strategy, DBRS, Fitch, Moody's, S&P

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