January 26, 2015

To: His Worship the Mayor
Members of City Council

From: Amber Smale, City Manager

RE: Debt Management Plan and Policy

RECOMMENDATION

1. That City Council approve the Debt Management Policy as outlined in Appendix A.

CONCLUSION

The Debt Management Policy is necessary to guide current and future decisions related to debt issued by the City of Estevan; and to establish parameters by which debt may be issued, the types and amounts of permissible debt, the timing and method of issuance that may be used and the procedures for managing outstanding debt.

Debt is integral for city operations when providing funding for long-term capital projects. Debt levels and their annual costs are important long-term obligations that must be managed within available resources. It is a limited resource that must be managed strategically in order to best support the City's priorities. Managing debt helps to improve the effectiveness of cash management, which, in turn, reduces cost and helps mitigate risks.

BACKGROUND AND DISCUSSION

Section 101(1)(f) of *The Cities Act* provides City Council with the ability to borrow money, lend money or guarantee the repayment of a loan pursuant to sections 133 to 153 of The Act. This is a matter Council may not delegate and requires the appropriate public notice be given.

The purpose of this report is to ensure Council has the information required to properly approve debt issuance along with a policy that will aid City Administration during future budget preparation.

The City of Estevan faces significant infrastructure needs over the next five years and beyond. The proposed capital programs (general capital and utility) total over $75 million over the next five years. These programs will only address the status quo and allow the City to begin a small annual capital program to address the immediate infrastructure needs in the community.

Over the next five years, the City will be faced with significant upgrades required at the Waste Water Treatment Plant of approximately $12-18 million. It is anticipated that a transportation study will identify the current need of an over/underpass given the increased flow of train traffic through the city. This project will likely be between $10-15 million. Both of these projects are significant and likely require the issuance of debt. The City's current debt limit is $55 million and therefore decisions need to be made carefully when planning for these projects.

In 2015, the City is again faced with challenges of past decisions and it's important that these matters be cleared up so that a more strategically planned program can be implemented. The City is faced with completing infrastructure work that was previously tendered and awarded, such as the Truck Route between 13th and 4th Street on 6th Street/Souris Ave, in the amount of $1.2 million. As well, the Ministry of Environment has issued legislative requirements that must be met in relation to the City's landfill site. A perimeter fence along with a geotechnical study and long-term ground water monitoring program has been ordered resulting in a cost of approximately $450,000. Further, the City is under a funding agreement with the Provincial Disaster Assistance Program that will result in a loss of $3.2 million if the City doesn't complete improvements to the Estevan Regional Airport in 2015 that resulted from the 2011 flood. This project is estimated at $5 million.

In order to meet these requirements, external financing is required and will aid the City in resolving these outstanding matters and puts the City in a better position to deliver a more balanced capital program in the future while also lessening the property tax burden.

In support of the 2015 budget cycle and planning, a debt management policy has been created and attached as Appendix A. This policy establishes the parameters for which public debt obligations will be undertaken by the City of Estevan. It reinforces the City's commitment to manage its financial affairs while minimizing risk and ensuring transparency and meeting the capital needs of the City.

A clear policy signals to the public, as well as lending agencies, that the City takes debt management seriously and is using policy to finance capital needs.

A Debt Management Policy is critical to enhancing the City of Estevan's long-term funding strategy in order to meet the future needs of Estevan residents. Debt is integral for city operations when providing funding for long-term capital projects. Debt levels and their annual costs are important long-term obligations that must be managed within available resources. It is a limited resource that must be managed strategically in order to best support the City's priorities. Managing debt helps to improve the effectiveness of cash management, which, in turn, reduces cost and helps mitigate risks.

The Debt Management Policy is necessary to guide current and future decisions related to debt issued by the City of Estevan; and to establish parameters by which debt may be issued, the types and amounts of permissible debt, the timing and method of issuance that may be used and the procedures for managing outstanding debt.

The Policy provides a framework for City Council to discharge their financial responsibilities and incorporates all applicable statutory requirements. It applies to all City of Estevan employees engaged in the budget process.

RECOMMENDATION IMPLICATIONS

Financial Implications

The Policy is intended to ensure all debt issuances and obligations are affordable and assessed using the debt affordability ratios identified in the policy. Annual debt servicing costs are factored into the general operating budget. The City's current debt repayment plan is as follows and this will be updated pending 2015 budget decisions.

Year	Principal	Interest	Balance at the end of the year
2015	3,763,069	1,000,946	28,378,687
2016	3,736,149	876,647	24,642,538
2017	3,872,538	739,064	20,770,000
2018	3,482,000	610,043	17,288,000
2019	3,603,000	492,373	13,685,000

Policy and/or Strategic Implications

A Debt Management Policy provides the City Administration with direction to effectively manage the City's debt. It will assure Council, staff and the public that debt is being administered effectively by:

- Clarifying options for long-term debt financing;
- Evaluation of the City's tolerance for risk of interest rate changes;
- Guide new financial decisions in terms of the preferred debt instrument and other portfolio operations; and
- Coordinate debt management decision making with asset management decisions to optimize overall funding and portfolio management strategies.

COMMUNICATION PLAN

This report and attached policy is available on the City's website.

DELEGATED AUTHORITY

The disposition of this report requires City Council approval.

Respectfully submitted,

Amber Smale
City Manager

CITY COUNCIL POLICY

Policy Title	Applies To		Reference #
Debt Management Policy	All employees engaged in budget process.		01-CC-15
Approved By	**Dates**		**Total # of Pages**
City Council	**Effective**		9
	Last Review		
	Next Review		
Authority	***The Cities Act***		
Distribution: Policy & Procedure Manuals, Copies to all Department Heads for circulation to staff.			

1.0 PURPOSE

The purpose of the City's Debt Management Policy is to:

- Guide current and future decisions related to debt issued by the City of Estevan
- Establish parameters by which debt may be issued, the types and amounts of permissible debt, the timing and method of issuance that may be used and the procedures for managing outstanding debt
- Integrate debt management with other long-term planning and financial and management objectives of the City
- Ensure the City maintains a sound financial position and that credit ratings are protected
- Restrict levels of debt incurred to approved debt limit and measures of affordability
- Maintain full and complete financial disclosure and reporting
- Establish debt that is affordable, sustainable, adaptable and supportive of the City's corporate priorities and long-term capital plans

Debt is a part of the City's financial structure and will be required for a longer-term financial management plan. Debt repayment will be structured based on fairness and equity for those who pay and benefit from the underlying asset over time.

All new debt must be approved by City Council and managed, monitored, and reported on annually by City Administration. Further, all debt service requirements shall be reviewed annually, and used to calculate overall annual debt affordability prior to expanding any capital program.

2.0 SCOPE

This policy applies to all City of Estevan employees engaged in the budget process.

3.0 DEFINITIONS

Balloon Maturity means a later maturity within an issue of bonds or debentures which contains a disproportionately large percentage of the principal amount that is repaid near the end of the debt term.

Bond means a debt security, in which the authorized issuer (City) owes the holders a debt and, depending on the terms of the bond, is obliged to pay interest to use and/or repay the principal at a later date (termed maturity).

Bullet Maturity means a maturity that has no payment until the stated maturity date

City means the City of Estevan.

Competitive Sale is a sale or auction of securities by an issuer in which underwriters or syndicates of underwriters submit sealed boxes to purchase the securities. This is in contrast to a negotiated sale.

Debenture and *Debentures* means a type of debt instrument that is not secured by physical asset or collateral. Debentures are backed only by the general creditworthiness and reputation of the issuer.

Debt means a monetary liability created by a financing agreement (e.g. note, debenture, bond, etc.) or a contingent liability such as that created by guaranteeing a monetary liability of another.

Debt Servicing means annual required debt repayments are made (including principal and interest).

Debt Term means the time period in which debt payments are made. At the end of the debt term, the debt is fully paid.

Derivative means a security whose price is dependent upon or derived from one or more underlying assets such as stocks, bonds, commodities, currencies, interest rates, and market indexes. The derivative itself is a contract between two or more parties and its value is determined by fluctuations in the underlying asset.

External Debt means all debt incurred by the issuance of term loans, debentures, and similar financial instruments.

Guaranteed Debt means borrowings or guarantees made by the City to a controlled or non-profit organization as per sections 151 to 153 of *The Cities Act*.

Internal Debt means funds loaned from existing civic reserves, in accordance with City policies, for the financing of capital projects.

Level Debt Service means debt (principal and interest) payments of equal amounts.

Long-term Debt means borrowings from third parties scheduled for repayment (i.e., generally with amortization over a period of one year or more).

Municipal Debt Limit means the City's debt limit as established by the Saskatchewan Municipal Board (currently at $55 million).

Negotiated Sale means a method of issuance in which the issuer (City) chooses an underwriter to negotiate terms pursuant to which the chosen underwriter will purchase and market the bonds.

Re-Designations mean changing the capital project that the debt is financing.

Saskatchewan Municipal Board is a Board that is legislatively mandated and empowered to exercise discretion of a regulatory and judicial nature. Among its mandate the Saskatchewan Municipal Board reviews local authorities' long-term debt applications for approval, to ensure financial stability and, to provide assurance of the local authority's financial stability to taxpayers and lenders.

Service Agreement Fee Credits means a financial commitment owed to a developer for work performed in relation to specifically agreed upon construction or performance within a service agreement.

Short-term Debt means debt which must be paid in full in less than 365 days.

Tax-supported Debt means all internal and external debt which is repaid totally or partially with the use of tax revenues.

Utility-supported Debt means all debt incurred from utility operation capital projects that will be repaid, together with interest, by a portion of the annual utility rates charged to utility customers.

Variable Rate Debt is debt with an interest rate that changes with the market.

4.0 POLICY

4.1 Legal Authority

All debt issues must meet the requirements of *The Cities Act,* and the municipal debt limit established by the Saskatchewan Municipal Board.

Debt issues must meet the standards for local government as prescribed by the Public Sector Accounting Board (PSAB) of the Canadian Institute of Chartered Accountants.

Debt approval and debt financing must follow all existing municipal policies, where applicable, and comply with the Debt Management Policy.

All long-term debt issuances must be approved by Council via a bylaw.

The City Treasurer has the delegated authority to create, amend and approve the Debt Management Policy once approved by City Council.

4.2 General Policy

Proceeds from debt issues are to be invested in accordance with the Investment Policy schedule.

All debt issued must be used for the specific purpose as outlined in the debt bylaw, unless Council directs otherwise via an amendment to the applicable debt bylaw.

4.3 Debt Limit and Affordability Measures

The City shall not issue new debt without conducting an analysis as to the City's ability to support the proposed additional debt service payments.

The City will assess the additional debt service requirements of any new debt including the percentage of debt being retired each year.

Debt is not to exceed the debt limit set by the Saskatchewan Municipal Board (currently at $55 million).

Short-term, long-term, guaranteed debt and Service Agreement Fee Credits are considered debt when comparing to the set debt limit.

Notwithstanding the limit prescribed in (3), prudent financial management suggests more stringent criteria to debt levels. The following ratios will assist in preserving borrowing capacity for future capital assets while maintaining flexibility for current operating funds:

> Debt Burden Percentage - This ratio measures the City's debt service burden as a percentage of total expenditures.
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> Debt Service Ratio - This ratio takes the percentage of annual interest and principal payments on debt to total City revenues.

If debt beyond the debt limit approved by the Saskatchewan Municipal Board is required, an application must be made by the City to the Board requesting approval of an increase to the existing debt limit.

4.4 Debt Issuance Process

Debt may be issued to acquire, construct, or remodel capital projects approved in the five year Capital Programs that cannot be funded from current revenue sources or for projects approved via subsequent Council resolution.

Debt may be issued for:

Tax-supported debt - Capital projects that will be serviced from the tax supported operating budget.

Utility-supported debt - Capital projects that will be serviced from revenues via the City's utility operations.

Debt issuance should achieve level debt service that matches the useful life of the capital asset being financed.

The City should avoid the use of balloon or bullet payments except in cases where the maturity serves to match a specific income stream and is within the overall debt limit and debt service level (as determine by the affordability measures).

Debt issuance via a competitive method of issuance, negotiated issuance, private placement or City administered process may be considered where it is found to be in the best interest of the City. A description of each sale process is as follows:

Competitive Sale – City bonds may be provided to the bidder that provides the lowest interest cost as long as the bid adheres to the requirements set forth in the official notice of sale. The City may consider a competitive sale where it is shown that it is in the best interest of the City.

Negotiated Sale – Under certain conditions, it may be favorable for the City to sell its debt obligations through a negotiated sale. The City may consider a negotiated sale where it is shown that it is in the best interest of the City.

Private Placement – The City may elect to privately place its debt. Private placement may be used where it is shown that there is a cost saving to the City relative to other methods of debt issuance.

City Administered – The City could also elect to issue and market its own debt, however, it would likely be more costly than the other three methods of debt issuance.

4.5 Debt Type

Short-term Debt (under one year) – Short-term debt will be used to finance short-term operational needs via a bank line of credit and short-term loans.

Long-term Debt (one year and over) – The City may use any of the following sources to fund long-term debt needs:

- Bonds
- Debentures
- Promissory Notes
- Term loans
- Finance Leasing
- Service Agreement Fee Credits
- Derivatives/Swaps
- Other securities (such as marketable and non-marketable bonds)

4.6 Debt Structural Features

Debt Denomination

The City will issue debt in Canadian dollars only.

Interest Rates

To maintain a predictable debt service burden, the City will generally give preference to debt that carries a fixed interest rate when issuing general obligation debt.

The City may consider variable rate debt if it is in the best interest of the City.

Interest rate swap agreements may be used to exchange floating-rate interest payments for fixed-rate interest payments if deemed appropriate by the City Treasurer.

Debt Financing

Debt will be issued for a capital project only where there is a fair allocation of debt costs between current and future beneficiaries or users, or in the case of an emergency capital need.

Debt will be issued on an individual capital project basis, the term of which will be influenced by the asset life of the capital project in question.

Long-term debt will not be used to finance current operating expenditures except in an emergency situation that is approved by Council.

Debt shall be structured to achieve the lowest possible net cost to the City given market conditions, the type of debt being issued, and the nature and type of the repayment source.

Asset Life

The City will consider long-term financing for the acquisition, maintenance, replacement, or expansion of capital assets only if they have a useful life of at least ten years.

City debt will not be issued for periods that exceed the useful life of the project to be financed.

Debt Repayment

Repayment term shall depend on the useful life of the asset being acquired by the City.

Unless otherwise warranted and deemed necessary by the City Treasurer, the repayment schedule should be structured to achieve level debt service for a debt issue.

Debt Re-Financing

The City may refinance (refund) outstanding long-term debt when refinancing allows for significant debt service savings.

City Administration will analyze outstanding long-term debt issues for debt service saving opportunities.

Debt refinancing should be considered in instances where the present value savings of a particular refinancing exceeds 3.0% of the present value of the debt service on the original debt issue.

The City may consider debt refinancing in circumstances where the primary objective is to eliminate any restrictive covenants that could have an impact on City operations.

4.7 Use of Derivatives

The use of derivative financial products will be considered if:

There is a reduction to the amount of interest rate risk or a lower cost of borrowing when used in combination with the issuance of bonds.

It enhances the relationship between the risk and return and provides the City with greater financial flexibility.

It generates interest rate savings and enhances investment yields.

The use of derivative financial products will not be considered if:

They are based on speculation regarding the future direction or level of interest rates (thus leading to unexpected leverage or risk).

The fair market value of the transaction cannot be readily and reliably determined at all times.

The transaction structure and terms will result in a lack of liquidity and the inability to timely terminate the transaction at market.

The City will consider all risk factors when determining whether to enter into a derivative transaction.

The City Treasurer shall only be authorized to enter into interest rate swap transactions with registered swap counterparties.

A report giving the status of any interest swap agreements entered into by the City will be provided to the City Manager in accordance with acceptable accounting standards.

5.0 APPROVAL AND ADMINISTRATION OF DEBT ISSUANCE

Debt funding for eligible capital projects will generally occur through the annual capital budget process.

Debt funding of emerging strategic priorities outside of the traditional budget process shall be approved by specific Council resolution.

Regardless of whether debt is approved through the budget or through a separate Council report, public notice, pursuant to *The Cities Act* is required to be provided in advance of the meeting where the debt will be considered.

All new debt issuance requests, re-designations of debt issuance, and revisions must be reviewed and approved by the City Treasurer prior to ratification by Council.

New debt issues will:

Be affordable, sustainable and maintain the City's financial flexibility;
Identify sources of funding for debt repayment;
Align with the City's capital plans and strategies and other financial and non-financial considerations;
Be pooled, when feasible, to minimize issuance costs.

5.1 Administration of Debt Transactions

All debt transactions (including debt servicing) shall be administered by the City Treasurer in accordance with current municipal policies, generally accepted accounting principles, and bylaws (including any conditions or restrictions placed upon the debt by the Administration and/or Council).

All debt accounts must be represented in the City's financial statements.

The Debt Management Policy will be reviewed annually by the City Treasurer to determine whether the debt limit and affordability measures are within the set targets.

Debt outstanding and repayment, as per the annual audited financial statement, should be compared to the debt limit and the level of affordability (as determined from the affordability measures presented in this policy).

Annual review and reporting will allow for any adjustments in the following year's budget cycle for meeting the debt limit and affordability measures.

6.0 ROLES AND RESPONSIBILITIES

City Council

Approves bylaws as it relates to debt issues
Provides authorization to the City Treasurer on an individually requested basis to negotiate external financing

City Treasurer

Approves the Debt Management Policy
Upon delegated authority from City Council, the City Treasurer negotiates with the City's fiscal agents to obtain external financing
Administers the Debt Management Policy
Administers the issuance of debt
Administers all debt transactions
Annually reports to Council the status of debt

7.0 REFERENCE MATERIAL

The Cities Act

8.0 REVISION HISTORY

Date	Description of Change	(Re) Approval Required