



The Corporation of the Town of Milton

Report To: Council

From: Glen Cowan, Chief Financial Officer / Treasurer

Date: May 30, 2022

Report No: CORS-042-22

Subject: Financial Securities - List of Authorized Institutions

Recommendation: THAT Town Policy 117 (Development Finance), be amended to expand the list of authorized financial institutions from which the Town of Milton will accept financial securities, as outlined in in Appendix 1 to this report.

EXECUTIVE SUMMARY

- As of 2021 year end, the Town held \$204 million in financial securities, \$198 million of which were in the form of letters of credit.
- The Town currently accepts letters of credit from only the six Schedule I Banks that are listed in Policy 117.
- The recommended expansion of the allowable financial institutions would more closely align the Town's policy with Halton Region, and would also provide additional flexibility for applicants of smaller projects.
- Although the expansion of allowable financial institutions will provide diversification in the number of organizations that the Town holds letters of credit from, it will result in a shift from the current practice towards institutions with lower credit ratings and overall asset bases. Additional administrative processes and demand on Town resources will also be created.
- The current expectation is that the majority of securities that are held by the Town will remain with Schedule I banks, and therefore the impacts of this change are expected to be manageable.

REPORT

Background

In 2020, Town Council approved Policy 117 to guide the development of agreements and provide a financial framework for growth in the community while protecting the Town's

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financial position. Section 4.2 of that policy pertains to financial securities, and provides staff the structure required to collect and administer those securities.

The Town requires the submission of financial securities in connection with the related approval processes or agreements including, but not limited to:

- Pre-servicing, servicing, subdivision, site plan, model home or condominium agreements
- Various financial agreements
- Site alteration, entrance, road occupancy, or road cut permit
- Encroachment agreements
- Local Stormwater Management Facility Monitoring Program
- Undertakings

As recently reported in report CORS-030-22, at 2021 year end the Town held \$204 million in total securities, of which \$198 million were in the form of letters of credit and \$6 million were in the form of cash securities.

Section 4.2.2 of Policy 117 outlines the institutions from which the Town will currently accept letters of credit as follows:

4.2.2 Acceptable Financial Institutions

In an effort to achieve a balance between the resources to support the policy and the decentralized intake of financial securities, the Town will only accept letters of credit from the following financial institutions set out in Schedule I of the Bank Act:

- Bank of Montreal
- Bank of Nova Scotia
- Canadian Imperial Bank of Commerce
- National Bank
- Royal Bank of Canada
- TD Canada Trust

In exceptional circumstances, letters of credit from other Schedule I banks may be accepted at the discretion of the Treasurer.

\$197.4 million in letters of credit held by the Town at 2021 were issued by the institutions noted above. The Town holds an additional \$0.6 million in letters of credit issued by other financial institutions that were grandfathered when Policy 117 was approved.

Based on a concern that was recently raised by an applicant that is involved in one of the Town's planning approval processes, as well as their financial institution, Town staff have revisited this policy as outlined in further detail below.

Discussion

As noted within the existing policy, the considerations involved in setting a policy framework include protection of the Town's financial position, the resources and administrative considerations in applying the policy, as well as the impact to stakeholders. By restricting the allowable institutions to the six Schedule I banks noted above, the Town has provided a simple and consistent framework for staff and applicants, and reduced credit exposure based on the size and credit rating of the allowable institutions. Cash securities also remained available as an option for applicants as an alternative to letters of credit.

As was noted in Halton Region report FIN-15-17, one potential challenge that may be associated with the current threshold for securities relates to the ability of relatively smaller scale projects that are undertaken by the residential and non-residential sectors, including specifically not-for-profit housing providers.

In order to address the challenge, Halton Region established a policy to allow financial securities as follows:

Halton Region Letter of Credit Policy (LOC) Excerpt:

A. Unless otherwise directed by Council, LOC will only be accepted by the Region from:

- Schedule I Banks: domestic banks authorized under Schedule I of the Bank Act to accept deposits; and
- Schedule II Banks: foreign bank branches of foreign institutions that have been authorized to under Schedule II of the Bank Act to do business in Canada

B. The Schedule I and II Banks must:

- Be federally regulated financial institutions under the Office of the Superintendent of Financial Institutions (OSFI) or its successor; and
- Have a credit rating of at least R-1 (Mid) as provided by the Dominion Bond Rating Service (DBRS) or an equivalent rating by one of the other acceptable agencies (i.e. Moody's or Standard and Poors).

C. LOC provided from Schedule I and II Banks do not have an upset limit.

Notwithstanding clauses A. B. C., an Additional Class of financial institutions will be maintained whereby a LOC may be accepted from a financial institution, provided that all of the following conditions are met:

- a. Financial institution must have a minimum of \$100 million in total assets;



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- b. The total value of LOCs accepted from individual financial institutions within this class shall be up to a maximum of \$2.0 million at the discretion of the Commissioner of Financial and Regional Treasurer (Treasurer); and
- c. The applicant within this class must provide all information required by the Treasurer in order for the Treasurer to determine the applicant's eligibility for the LOC.

In the event that a financial institution fails to maintain eligibility, the Region may require a new LOC from an acceptable financial institution. This LOC will be provided to the Region within 30 days of the request. If the replacement LOC is not received, the Region reserves the right to immediately draw upon the original LOC.

As noted above, Halton Region's policy allows for financial securities from a much broader list of institutions than the Town's current framework. Of particular note, the "Additional Class of Financial Institution" that is noted in the policy creates an avenue for the Region to accept securities that are issued by Credit Unions. The policy also limits the Region's overall exposure to these Additional Classes by restricting the total allowable exposure to \$2.0 million per institution, establishing minimum asset requirements, and allowing the Region to draw on the security if required.

Should the Town adopt a policy that more closely resembles the Region's, the alignment should lead to more consistency to applicants that deal with both levels of government when developing within the Town. There are several internal considerations for the Town, including:

- **Alignment with Investment Policy**

The Town's investments are managed through a Treasury Policy (Policy 116). Similar to the financial securities that are managed via Policy 117, credit risk is a key consideration for investments as well. Policy 116 allows the Town to invest in Schedule I and Schedule II banks, as well as Credit Unions, where a minimum credit rating of R-1 (low) for short term and A (low) for long term. These ratings are associated with companies that are considered to have good credit quality, in that their capacity for the payment of financial obligations is substantial. They may be vulnerable to future events, but qualifying negative factors are considered manageable.

As such, an expansion of the allowable financial institutions in Policy 117 would generally align with the credit exposure that is allowed for in Policy 116.

- **Administrative Considerations**

A key difference in administering Policy 117 relative to Policy 116 is the number of individuals involved in the process, which will have an effect on the design of the related procedures and controls. The Town's investments are managed by a

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limited group of staff who have knowledge specific to credit ratings and the associated financial risk and considerations. The letters of credit that the Town receives, on the other hand, involve a broader group of staff from several department areas, numerous external stakeholders, varying size of securities, and more unpredictable frequencies.

These differences will need to be factored into any protocols that are established to ensure that the appropriate validations have occurred prior to the acceptance of securities and the related application/permit approvals.

The introduction of limits, either in the form of the minimum assets held by the allowable financial institutions, credit rating or in the total financial securities held by the Town from any specific institution, will create additional demands on Town staff. These impacts will be monitored and assessed in relation to the degree that the expanded list of institutions are utilized, as well as the resulting benefits.

- **Impacts to the Town's Risk Profile**

Adoption of a financial securities policy that more closely resembles Halton Region's will result in a diversification of the financial assets held by the Town. At this time, staff expect that the vast majority of securities held will continue to be received from the primary Schedule I Banks the Town currently deals with.

With this diversification, the Town will see a portion of the financial securities held shift to financial institutions that will likely have a lesser credit rating and fewer assets held than the Town's current experience.

These expected trends will be monitored to understand the degree of the potential shift that occurs, and further detail can be reported through the Town's annual update report from the Development Finance business unit.

Recommendation

Based on this review, staff recommend an update to the Town's Development Finance policy to expand the list of allowable financial institutions as well as adjust the roles and responsibilities to accommodate a broader list. The proposed policy language is attached as Appendix 1. All other elements of the Town's policy are recommended to remain as currently written, including the forms of financial security, the requirements for standby letters of credit, and the conditions on which the Town will draw or release a financial security.

Although the proposed policy includes elements from Halton Region's, several specific amendments were made. The first pertains to the criteria for the Additional Class of financial institution. Rather than establishing a measure based on minimum assets of \$100 million, the Town's proposed policy includes language that aligns with the criteria for credit unions with that of Ontario Regulation 438/97. Specifically, based on the most



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recent audited financial statements, the allowable institutions in the “Additional Class” must have:

- Positive retained earnings;
- Regulatory capital of at least the percentage of its total assets set out in subsection 2.0.3 of O.Reg 438/97;
- Regulatory capital of at least the percentage of its total risk weighted assets set out in subsection 2.0.4 of O.Reg 438/97; and
- Positive net income for three of its five most recently completed fiscal years.

Alternatively, the financial institution must carry a credit rating that is equivalent to the Schedule I or Schedule II banks that the Town would accept a letter of credit from. These measures have been recommended as an alternate threshold as they provide a better measurement of the institution’s ability to honour the financial commitment to the Town should the letter of credit need to be drawn upon.

The other alteration to the policy pertains to the \$2 million limit per institution under the Additional Class. The policy language was amended to clarify that the Town’s Treasurer has the authority to vary from the stated limit, at their discretion. Although the \$2 million threshold is expected to be sufficient in most cases, this measure will provide some flexibility to respond to potential scenarios that may arise as the Town puts the new framework into practice.

Financial Impact

The establishment of a strong financial policy framework is critical to supporting sound decision making in support of Council’s strategic priorities and vision for the community.

The recommendations contained herein will result in the expansion of allowable financial institutions, including those with a lower credit rating and fewer total assets than the Town’s current policy. There will be additional administrative demands on the Town to implement the recommended policy as well. Despite these factors, a policy update is recommended with consideration for the needs of the Town’s stakeholders (including potential not-for-profit affordable housing or purpose-built rental unit developments) and the degree these additional institutions are expected to be utilized.

Monitoring of the impacts of this policy change will occur and be reported to Council through the annual reporting of the Development Finance business unit.

Respectfully submitted,

Glen Cowan



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Chief Financial Officer / Treasurer

For questions, please contact: Melanie Wallhouse, Manager, Phone: Ext. 2314
Development Finance and
Financial Consulting

Attachments

Appendix 1 - Proposed Amendment to Policy 117 - Development Finance

Approved by CAO
Andrew M. Siltala
Chief Administrative Officer

Recognition of Traditional Lands

The Town of Milton resides on the Treaty Lands and Territory of the Mississaugas of the Credit First Nation. We also recognize the traditional territory of the Huron-Wendat and Haudenosaunee people. The Town of Milton shares this land and the responsibility for the water, food and resources. We stand as allies with the First Nations as stewards of these lands.

Appendix 1 - Proposed Amendment to Policy 117 - Development Finance

Existing Language:

4.2.2 Acceptable Financial Institutions

In an effort to achieve a balance between the resources to support the policy and the decentralized intake of financial securities, the Town will only accept letters of credit from the following financial institutions set out in Schedule I of the Bank Act:

- Bank of Montreal
- Bank of Nova Scotia
- Canadian Imperial Bank of Commerce
- National Bank
- Royal Bank of Canada
- TD Canada Trust

In exceptional circumstances, letters of credit from other Schedule I banks may be accepted at the discretion of the Treasurer.

Amended Language:

4.2.2 Acceptable Financial Institutions

A. Unless otherwise directed by Council, letters of credit will only be accepted by the Town from:

- Schedule I Banks: domestic banks authorized under Schedule I of the Bank Act to accept deposits; and
- Schedule II Banks: foreign bank branches of foreign institutions that have been authorized to under Schedule II of the Bank Act to do business in Canada

B. The Schedule I and II Banks must:

- Be federally regulated financial institutions under the Office of the Superintendent of Financial Institutions (OSFI) or its successor; and
- Have a credit rating of at least R-1 (Mid) as provided by the Dominion Bond Rating Service (DBRS) or an equivalent rating by one of the other acceptable agencies (i.e. Moody's or Standard and Poors).

C. LOC provided from Schedule I and II Banks do not have an upset limit.

Notwithstanding clauses A. B. C., an Additional Class of financial institutions will be maintained whereby a letter of credit may be accepted from a financial institution, provided that all of the following conditions are met:



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- Financial institution must have a credit rating of at least R-1 (Mid) as provided by the Dominion Bond Rating Service (DBRS) or an equivalent rating by one of the other acceptable agencies (i.e. Moody's or Standard and Poors);

OR

Financial institution must have, based on the most recent audited financial statements, each of the following:

- Positive retained earnings;
- Regulatory capital of at least the percentage of its total assets set out in subsection 2.0.3 of O.Reg 438/97;
- Regulatory capital of at least the percentage of its total risk weighted assets set out in subsection 2.0.4 of O.Reg 438/97;
- Positive net income for three of its five most recently completed fiscal years; and

The financial institution may be required to certify in writing that all of the financial indicators mentioned in subsection 2.0.2 of O.Reg 438/97 are met by the credit union or central.

- The total value of letters of credit accepted from individual financial institutions within this class shall be up to a maximum of \$2.0 million or as otherwise determined at the discretion of the Town Treasurer; and
- The applicant within this class must provide all information required by the Town Treasurer in order for the Treasurer to determine the applicant's eligibility for the Letter of Credit.

In the event that a financial institution fails to maintain eligibility, the Town may require a new letter of credit from an acceptable financial institution. This letter of credit will be provided to the Town within 30 days of the request. If the replacement letter of credit is not received, the Town reserves the right to immediately draw upon the original letter of credit.

The following responsibility will also be added to Section 5. Roles and Responsibilities:

Individual(s)	Responsibilities
Financial Planning and Policy Business Unit	ii. Evaluate and confirm financial institution eligibility for letters of credit authorized under section 4.2.2.