ITEM # 4.2

HRWC Board

March 26, 2020

TO: Craig MacMullin, MBA, CPA, CGA, Chair, and Members of the Halifax Regional Water Commission Board

SUBMITTED BY: Digitally signed by Louis de Montbrun Date: 2020.03.20 11:50:26 -03'00'

Louis de Montbrun, CPA, CA, Director, Corporate Services/CFO

APPROVED: Cathie O'Toole Digitally signed by Cathie O'Toole DN: cn=Cathie O'Toole, o=Halifax Water, ou=General Manager, email=cathieo@halifaxwater.ca, c=CA Date: 2020.03.19 22:50:59 -03'00'

Cathie O'Toole, MBA, FCPA, FCGA, ICD.D, General Manager

DATE: March 16, 2020

SUBJECT: **2020 Spring Debenture**

ORIGIN

Halifax Regional Water Commission (Halifax Water) participation in the Spring 2020 Municipal Finance Corporation (MFC) debenture issue to secure debt financing for 2019/20 additions to utility plant in service.

RECOMMENDATION

It is recommended that the Halifax Water Board:

1. Approve the financing of $25,000,000 for a ten year term with a twenty year amortization schedule and an all-inclusive rate not to exceed 5.5%.
2. Approve the financing of $1,700,000 for a ten year term with a ten year amortization schedule and an all-inclusive rate not to exceed 5.5%.

BACKGROUND

Halifax Water is legally required to borrow through the MFC. The borrowing proposed in this report is estimated based on the Five Year Business Plan, the approved Operating and Capital Budgets for 2019/20 and 2020/21, and the rate schedule approved by the Nova Scotia Utility and Review Board.

DISCUSSION

Long term debt issued for capital projects is normally amortized for a period of twenty years based on the life of the assets being financed. Traditionally the market for twenty year financing in Canada has been more expensive than ten year financing so twenty year amortized debt is usually financed for ten years and the balloon payment refinanced for the remaining ten years. Though a lower interest rate cost is secured for the first ten years, there is a risk that interest rates will be higher at the time the balloon payment is due for refinancing.

The 2019/20 Capital and Operating Budgets were prepared based on funding that included $39.9 million of debt to finance water, wastewater and stormwater additions to utility plant in service. Based on the timing of capital expenditures and cash flow projections, the full amount of the planned debt is not required; only $25.0 million in new debt will be issued at this time.

An additional $48.5 million of debt is planned to fund the 2020/21 Capital Budget. This is expected to be issued in either Fall 2020 or Spring 2021. The acquisition of debt following completion of capital projects aligns with the expectations of MFC.

The $25.0 million will be applied to Water, Wastewater, and Stormwater as follows:

Water	$12.0 million
Wastewater	$7.4 million
Stormwater	$5.6 million

In addition to the new debt required, a balloon payment is also due on an existing debt issue. In 2010/11, new debt of $3.4 million was acquired to fund wastewater capital expenditures. Debt was acquired for a ten year term with a twenty year amortization. A balloon payment of $1.7 million is due June 29, 2020, which will be refinanced for the remaining ten years.

The new issue can be expected to have a lower interest rate than the original issue. The 2010 Debenture had an interest rate of 3.70%. Our current Weighted Average Cost of Debt is 3.22% and the Fall 2019 Debenture had an interest rate of 2.61%.

The final interest rates and timing of the debt issues will not be known with certainty until the formal debenture process concludes.

Halifax Water's debt is covered by a blanket guarantee approved by Halifax Regional Municipality (HRM) Council in September 2014. The blanket guarantee will apply to all Halifax Water debt with a condition that Halifax Water must maintain a debt service ratio of 35% or less. Halifax Water's debt service ratio is 18.46% as of February 29, 2020. The debt service ratio is calculated as the cost of debt interest, principal and discount payments

divided by the total Operating Revenue as found on the income statement (NSUARB format).

Halifax Water's outstanding debt at March 31, 2019 (including the current portion) was $208.3 million, and debt is projected to be $220.1 million at March 31, 2020.

BUDGET IMPLICATIONS

The 2020/21 budget includes $30.7 million in debt servicing. Halifax Water's capital financing strategy is designed to maintain a debt service ratio of 35% or less; and to use a mixture of infrastructure funding, development related charges (reserves), depreciation, and debt.

ALTERNATIVES

1. Halifax Water could choose to forgo participation in the 2020 Spring Debenture and defer issuance of debt until fall 2020, however there is not sufficient cash available for forecasted expenditures over this timeframe.
2. The full twenty year financing could be secured at a higher cost in the near term to avoid the risk of higher interest rates when the debt is to be re-financed after ten years.

ATTACHMENTS

1. Borrowing Resolution for $25.0 million of new debt and $1.7 million for debt renewal.
2. Cash Flow Model for 2020/21 based on approved Operating and Capital Budgets and anticipated cash flow.

Report prepared by: Alicia Scallion

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