SUBJECT: **Pay-On-Demand Development Bonds Policy**

TO: **Pipeline to Permit Committee**

FROM: **Finance Department**

Report Number: F-28-24

Wards Affected: not applicable.

Date to Committee: November 7, 2024

Date to Council: November 19, 2024

Recommendation:

Approve the Pay-On-Demand Surety Bond Policy and the Pay-On-Demand Surety Bond Template attached as Appendix A to finance department report F-28-24; and

Approve the amended Letters of Credit Policy and Letter of Credit template attached as Appendix B to finance department report F-28-24; and

Authorize the Chief Financial Officer to make amendments to Appendix A and the attachment thereto if required to comply with provincial legislation; and

Authorize the Commissioner of Legislative Services and City Solicitor to amend any contractual language in development agreements related to the acceptable forms of security if required to comply with provincial legislation.

PURPOSE:

The purpose of this report is to respond to the following recommendations approved by Council on June 18, 2024, as part of Finance report F-13-24.

> *Approve a five (5) development pilot program approach to accepting Pay-on-Demand development bonds that considers a number of bonds per developer and maximum bond amount that is satisfactory to the CAO; and,*
>
> *Direct the Chief Financial Officer to develop a pay-on-demand bond template and pay-on-demand development Bond Policy in accordance with the approved five (5) pilot program, in a form satisfactory to the Executive Director of Legal and*

Corporation Counsel, as outlined in this report for Council approval by Fall 2024; and,

Direct the Executive Director of Legal and Corporation Counsel to ensure that Site Plan Agreements for developments participating in the pilot program recognize pay-on-demand development bonds as an acceptable form of security, as recommended in this report; and,

Responses to the following approved recommendations will be provided through future reporting to the Pipeline to Permit (P2P) Committee:

Direct the Chief Financial Officer to maintain a waitlist of additional developments above the five accepted and report back monthly to the Pipeline to Permit Committee on the additional developments; and

Direct the Chief Financial Officer to report back in one (1) year, or earlier subject to provincial legislation or pilot program demand with a summary of challenges and future consideration for on-going acceptance of Pay-On-Demand development bonds or pilot program expansion; and,

Staff will report back on the following direction in Q1-2025, as staff have been working towards initiating the pilot program herein and responding to provincial legislation on bonds.

Direct the Chief Financial Officer to connect with the industry and report back to the Pipeline to Permit Committee by the end of Q4 2024 on how to incorporate the option of transferring letters of credit to surety bonds.

The report provides an overview of parameters and city policy required in order to accept pay-on-demand surety bonds (bond) at the City of Burlington. The city intends to run a pilot for acceptance of pay-on-demand surety bonds for a maximum of five (5) developments bringing forward a site plan application to minimize risk to the city in accepting bonds.

Vision to Focus Alignment:

- Increase economic prosperity and community responsive city growth

---

Executive Summary:

The report herein is being brought forward for Council to approve a bond policy and bond template for the acceptance of pay-on-demand surety bonds. The approach allows the city to accept pay-on-demand surety bonds for a maximum of five (5) new site plan agreements. The parameters discussed at P2P in June 2024 in regard to a bond value threshold and limitations on the number of bonds per developer have been removed. The

city's existing options of letters of credits and cash securities continue to be available. The report requests approval of the appendices outlining a required bond template and bond policy to initiate the program. The report also recommends approval of housekeeping amendments to the Letters of Credit policy. Transition of existing securities is not part of this pilot.
A pilot program allows staff the opportunity to learn, develop and refine processes as it relates to bonds and learn how this can be adapted to other municipal land-use planning agreements.
To support possible future legislation that will be resulting from Ministry Municipal Affairs and Housing (MMAH) consultation and feedback of Ontario municipalities on ERO 019-9198, the report recommends authorizing: the Chief Financial Officer to make amendments to the pay-on-demand surety bond policy and pilot program, including terminating the pilot program if required by provincial legislation; and, the Commissioner of Legislative Services and City Solicitor to make amendments to development agreements, as required to implement provincial legislation.

Background and Discussion:

The city currently accepts either a letter of credit (LC) or cash as security for agreements related to Planning Act approvals. This security represents a portion of the cost of municipal related construction work (sewers, grading, stormwater management, related site management etc.) and is held by the city until the agreed upon work has been completed to the satisfaction of the city.

A Letter of Credit is a form of security issued by a financial institution that guarantees payment or performance by allowing the city the right to draw upon the security in the case of developer default. The LC as a security instrument continues to be widely and most commonly used by municipalities due to its ease of use and presents the least financial risk to the municipality.

To further mitigate the inherent risk that is attached to an LC, the city follows the Letter of Credit Policy. This policy provides a framework that is to be followed when accepting LCs. As part of this process, staff have undertaken a review of the existing LC policy and template and have made minor revisions to address common practice for Council approval, attached as Appendix B.

Strategy/process/risk

The primary reason behind implementing this pilot program is that the city's current policy of accepting only letters of credit is considered limiting to developers and is viewed as tying up funding and borrowing capacity for developers. As financial securities have evolved over time, the features of a pay-on-demand surety bond appear to align with the features of LCs. The most notable difference is as follows:

- Surety bond is held with an insurance company as opposed to a financial institution. However, the insurance industry is regulated by the Financial Services Regulatory Authority of Ontario (FSRA) and is subject to credit ratings.

Though this appears to be only a singular difference it is important. The bond is an insurance product, backed by an insurance company, as opposed to financial instrument regulated by a Canadian financial institution, and fully backed by cash collateral.
Staff outlined the following risks as it pertains to bonds in report F-13-24, (Pipeline to Permit, June 13, 2024):

- The policy includes a minimum credit rating for surety providers to ensure company's solvency, financial strength, and ability to pay claims. However, if the number of municipalities accepting bonds increases it may dilute the ratings.
- Administratively difficult to monitor any changes in credit ratings based on future volume and change in financial strength.
- Concern that payment would not be disbursed or that a municipality would need to spend extended amounts of time proving default prior to accessing funds through a surety bond.
- Municipalities have not yet had any experience with a claim to date, nor judicial guidance therefore it is unknown if payments on claims in fact are timely and administered with ease.
- Uncertainty around the level of financial consequence to the developer that would alleviate the need for regular inspections to decrease the security amount and potentially the need for developers to address deficiencies in a timely manner.
- The lack of experience with demand bonds in the development application context means that outcomes where security needs to be drawn upon cannot be fully predicted.

On September 7, 2024, the Toronto Star published an article, "When Builders Go Bust," which highlighted the financial woes being experienced by many housing developers. The article indicates that at least 27 Ontario developers have gone into receivership this year and expect the trend to continue as builders tackle an unstable economic landscape, in the form of labor shortages, high interest rates and high materials costs. The message in the article reinforces the high level of risk in the development industry, thereby lending to the importance of having securities backed by cash collateral in place which will provide the least risk to the city in these cases.

Pilot Program:

The pilot program for the acceptance of the bond for a maximum of five (5) site plan agreements is to minimize financial and legal risk to the city. The pilot program will run for a two-year period, beginning on November 19, 2024, and ending on November 19, 2026, unless directed otherwise by Council or provincial regulation. Furthermore, in the city's due diligence with other municipalities site plans applications seemed to be the predominant case for the use of bonds. Overall, the city's bond policy and template, included as Appendix A, are generally in alignment with other municipalities the city has had discussions with. Some key parameters included within the policy are as follows:

- A minimum credit rating of "A-" as assessed by Standard & Poor's or an equivalent rating from Fitch Ratings of "A-" (high credit quality), Moody's Investors ("A3"), A.M. Best Company, Inc., of "A" or higher, or "A" or higher as assessed by Dominion Bond Rating Service.
- The issuing surety provider must be an active institution monitored by the Financial Services Regulatory Authority of Ontario.
- Inspections are requested by applicants on a regular interval to decrease the Security amount, hereby continuing the incremental monitoring practiced with Letters of Credit.
- An individual Bond's scope is limited to a singular project, allowing for a direct relationship with security and project and it allows to track projects better.

The province has been consulting on potential regulation to specify the type of instruments to be used to secure municipal land use planning approvals, including surety bonds. Proceeding with a pilot program will allow staff to more readily align the bond policy and template to impending future legislation.

The timing of release of the proposed regulation is currently unknown. Should the regulation come into effect prior to November 19, 2026, amendments would be required to bring the bond policy and template into compliance with the regulation. It is recommended that the Chief Financial Officer and Commissioner of Legislative Services and City Solicitor be authorized to make any changes to the existing documentation required to implement the regulation.

Financial Matters:

There are no financial impacts in development of a pilot program for pay-on-demand surety bonds. However, there is a risk of financial impact in consideration of future claims that maybe required.

Climate Implications:

Not Applicable.

Engagement Matters:

The following is an outline of engagement that occurred throughout the process:

- March 8, 2024, Marsh Canada provided a presentation to city's Pipeline to Permit Committee.
- April 25, 2024, staff met with WEHBA, and Marsh as part of staff's initial report to Pipeline to Permit Committee on June 13, 2024.
- Staff have conducted a series of meetings with the following municipalities who are currently accepting these instruments as security in development of the bond policy and template. Staff have carefully reviewed their policies and templates and consider its contents consistent with city policy attached as Appendix A, ensuring there is regional alignment in practice and policy.
    - Halton Hills
    - City of Guelph
    - City of Hamilton
    - City of Ottawa

On September 16, 2024, the Ministry of Municipal Affairs and Housing (MMAH) released ERO 019-9198 that includes proposals for future regulation that would authorize homebuilders to use a pay-on-demand surety bond with prescribed features. The city has provided comment to the ERO prior to the closing period (October 16, 2024). The province proposed the following proposed mandatory elements of a pay-on-demand surety bond.

Licensing Requirement	Bond would be required to be issued by an insurer that is licensed under the *Insurance Act* and overseen by the Financial Services Regulatory Authority of Ontario (FSRA).
Credit Rating Requirements	The insurer would be required to meet specified posted credit ratings.
Guaranteed Payment	The insurer is obligated to make payment to the municipality for the amount demanded, in event the principal has defaulted on the obligation.

Timely Payment	The insurer is obligated to make payment to the municipality within 15 business days of written notice of default.
Partial Drawdowns	The municipality may release portions of the security when the condition of development has been fulfilled.
Cancellation	The insurer would be required to provide written notice to the municipality and the principal at least 90 days in advance of its intention to terminate the pay-on-demand surety bond.

Overall, staff's comments are supportive of the proposed mandatory elements keeping in mind the risks that were highlighted as part of the June report to P2P (F-13-24). The city's bond policy and template attached for Council approval are generally in alignment with all elements as currently proposed by the province.

Conclusion:

As directed by Council, attached are a bond policy and bond template to initiate the pilot program for the acceptance of pay-on-demand surety bonds for future site plan applications agreements. Staff will come forward with subsequent reports based on approved report recommendations contained in report F-13-24. Minor amendments to the Letters of Credit Policy are also recommended, as is authority for the Chief Financial Officer and Commissioner of Legislative Services and City Solicitor to make amendments to the pay-on-demand surety bond policy and development agreements respectively, as may be necessary to implement provincial legislation.

Respectfully submitted,

Reena Bajwa

Manager of Financial Strategies & Business Consulting

905-335-7600 ext. 7896

Appendices:

A. Bond Policy and Template
B. Letter of Credit Policy and Template

Report Approval:

All reports are reviewed and/or approved by Department Director, the Chief Financial Officer and the Commissioner of Legislative Services and City Solicitor.