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Report 2024-158

Report Title: Golden Plough Lodge & Northumberland County Archives and Museum Redevelopment Project Financing

Committee Name: Finance and Audit

Committee Meeting Date: December 3, 2024

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Director of Finance/Treasurer
Finance

Approved by: Jennifer Moore, CAO

Council Meeting Date: Select Council Meeting Date

Strategic Plan Priorities: Innovate for Service Excellence
 Ignite Economic Opportunity
 Foster a Thriving Community
 Propel Sustainable Growth
 Champion a Vibrant Future

Recommendation

That the Finance and Audit Committee, having considered Report 2024-158 ‘Golden Plough Lodge (GPL) and Northumberland County Archives and Museum (NCAM) Redevelopment Project Financing’, recommend that County Council direct staff to finalize the current approved debenture with Ontario Infrastructure and Lands Corporation in the amount of \$96,770,321 with a term of _____ years; and

Further That the Committee recommend that County Council identify the additional financing requirements for the GPL and NCAM project for separate discussion during budget deliberations at the December 18th, 2024 County Council meeting.”

Purpose

The purpose of this report is to:

1. Provide County Council with an update on the GPL & NCAM Project financing
2. Provide Council with options for funding the projected shortfall in financing, and
3. Request approval from Council to begin the process of finalizing the initial debenture with Ontario Infrastructure and Lands Corporation (IO) for the existing approved debenture in the amount of \$96,770,321.

Background

Northumberland County and Matheson Constructors Limited (MCL) entered into a contract for the construction of the GPL & NCAM redevelopment project on December 4, 2020. The original budget for the total project was \$115,428,999.

The majority of the financing comes from a debenture with IO that has been approved at a maximum amount of \$96,770,321. This is the maximum amount that can be obtained from IO through this loan. The County can apply for another loan from IO to cover additional costs, but this would have to be a separate application and loan.

The updated total project costs are estimated to be \$144,487,330 as of October 31, 2024.

The expected financing sources for the project are outlined below:

<u>Funding Source</u>	<u>Amount (\$)</u>	<u>Comments</u>
IO Debenture	96,770,321	Maximum from current loan
Reserves (Rebuild)	10,389,281	Projected
Reserves (Rebuild)	3,666,558	Used in 2019 and prior
Reserves (Archives)	500,000	Projected
Reserves (Corporate)	9,410,887	Interest on construction financing (Estimate)
Development Charges	1,983,462	Estimate
MOHLTC Planning Grant	250,000	
MOHLTC Market Segment Grant	4,236,140	
Federal Cultural Spaces (NCAM)	295,000	
Levy	387,500	2019 and prior
TOTAL	127,889,150	

The difference between the projected total cost and the projected financing is \$16,596,025. Council must decide how to finance this additional amount.

It is important to note that this unfinanced amount is not the same as the difference between the original budget and the current projected cost because corporate reserves are being used to cover the construction financing interest costs and because the original principal amount of the IO debenture was larger than was needed to leave room for contingency costs.

This project was started in the first year of the COVID 19 Pandemic. The Bank of Canada (BOC) lowered its overnight lending rate to 0.25% at the beginning of the pandemic in an effort to stimulate the economy. After two years of low interest rates, Canada (and many other countries) experienced record inflation starting in March of 2022 and the BOC responded by raising its overnight lending rate dramatically until it reached to 5.0%.

Long-term bond rates rose during this time. The IO rate for a 25-year loan was 4.73% on October 31st, 2022. Between October 2022 and November 2024 the 25-year IO rate has remained in this range with some minor fluctuations. Staff have been closely monitoring the bond rates during this time because of its impact on the overall interest that will be paid to IO over the life of the loan.

The IO rate for a 25-year loan is 4.50% as of November 14, 2024.

Consultations

Staff have consulted with the County's investment advisors at The Johnson, Johnston and Macrae Investment Group (CIBC Wood Gundy) on matters relating to economic conditions, forecasts and the bond market.

Legislative Authority / Risk Considerations

Interest Rate Risk

The amount of interest expense that will be incurred by Northumberland County over the life of this loan is dependent on the interest rate that will be in effect when the debenture is finalized. These rates are tied to the bond market, and we do not have any control over the rate that will be charged.

Historically, Northumberland has finished the construction of project before finalizing a debenture with IO. It is possible to finalize a debenture early (before the completion of construction) but we must give 60 days' notice in order to do this.

The bond rates are constantly changing and there is a risk that they will change between when a decision is made by council and when the debenture is finalized. They could also change dramatically after the debenture is finalized. Changes in market conditions or in the geopolitical situation can potentially have a dramatic effect on the bond rates.

Discussion / Options

The Existing IO Debenture for the GPL & NCAM Project

Northumberland County has an agreement with IO and must finalize its current debenture for the GPL & NCAM project by June of 2025. There is the possibility of extending this deadline by

a year with approval from IO. Once substantial completion is reached the debenture must be finalized within 120 days.

Finance staff have been closely monitoring the IO interest rates over the last two years since it reached a high of approximately 4.75%. The 25-year IO rate has remained relatively unchanged over this period. This rate is at 4.5% as of November 14, 2024.

Our financial advisors are projecting that long-term bond rates are going to start to increase again in 2025. Based on this information, staff are recommending that Council direct staff to immediately begin the process for finalizing the existing debenture for the GPL & NCAM project in the amount of \$96,770,321. The opinion from our financial advisors is based on their examination of current market conditions and while unexpected changes in economic (or geopolitical) conditions can have a significant impact on rates, this is the best information that we have at this time.

Term of the Debenture

Historically the County has used a 25-year term for IO debentures for buildings. However, Council has the option of reducing the term (with IO’s approval) from 25 to 20 years. The semi-annual payments would increase but the total amount of interest paid over the life of the loan would decrease dramatically because the principal is being paid back faster.

IO loans have two semi-annual payments. If the debenture is finalized in the first half of 2025, then there will be one payment in the second half of 2025 and then two payments in 2026 and going forward.

Based on a principal amount of \$96,770,321 the following shows the impact on the payments, the 2025 and 2026 budget impacts and total interest of the two different terms:

	25-Year Term (4.50%)	20-Year Term (4.43%)	Difference
First Half-year payment (2025)	\$3,243,582	\$3,672,249	\$428,667
% Impact on 2025 Levy	4.38%	4.96%	0.58%
Full Year payment (2026)	\$6,487,165	\$7,344,498	\$857,333
% Impact on 2026 Levy	3.96%	4.48%	0.52%
Total Lifetime Interest	\$65,408,796	\$50,119,638	(\$15,289,159)

By moving to a 20-year term the County would save \$15,289,159 on a principal amount of \$96,770,321 at current debenture rates. If Council would prefer to proceed with a 20-year term, then staff need to inform IO of the requested change.

Additional Financing Required for the GPL & NCAM Project

As mentioned in the background section, County Council must decide how to finance the additional cost of \$16,596,025 for the GPL & NCAM project. The two main options available to Council are another debenture from IO, draws from reserves, or some combination of the two. There is the potential for there to be surpluses in 2024 and 2025 that could be used to help offset the costs but these are not guaranteed.

The following section shows the total payments and interest if the County were to apply for a second debenture from IO to finance an extra \$8M, or an extra \$16.6M. Any amount below \$16,596,025 would need to be covered by a transfer from reserve or another source. A full sensitivity analysis of different principal amounts can be found in Attachment 1.

Note: The chart below is based on a 25-year term

Principal	\$96,770,321 (Current Amt)	\$104,770,321 (\$8M extra)	\$113,339,346 (\$16.6M extra)
First Half-year payment (2025)	\$3,243,582	\$3,511,729	\$3,798,949
% Impact on 2025 Levy	4.38%	4.74%	5.13%
Full Year payment (2026)	\$6,487,165	\$7,023,458	\$7,597,898
% Impact on 2026 Levy	3.96%	4.28%	4.63%
Total Lifetime Interest	\$65,408,796	\$70,816,140	\$76,608,098

Note: The chart below is based on a 20-year term

Principal	\$96,770,321 (Current Amt)	\$104,770,321 (\$8M extra)	\$113,339,346 (\$16.6M extra)
First Half-year payment (2025)	\$3,672,249	\$3,975,834	\$4,301,012
% Impact on 2025 Levy	4.96%	5.37%	5.80%
Full Year payment (2026)	\$7,344,498	\$7,951,667	\$8,602,024
% Impact on 2026 Levy	4.48%	4.85%	5.25%
Total Lifetime Interest	\$50,119,638	\$54,263,027	\$58,701,128

Alternatively, the unfinanced amount could be financed with a draw from reserves. Amounts could be drawn from the County's General Reserve and/or borrowed (or redirected) from amounts in other reserves that have previously been committed to other uses. Any reserve

amounts used will reduce the amounts available for other projects and will reduce the amount of interest revenue generated from investments.

The County is currently earning 4.35% on its investments in its high interest savings account (HISA). The Bank of Canada (BOC) is expected to reduce its overnight lending rate a further 1.5% by the middle of 2025. This will further reduce the amount that the County will earn on the funds in its HISA account. Given this expected spread between what the County will earn on the investments (in its HISA account) and the 4.5% interest on the IO 25-year debenture, an argument can be made for using reserve funds to finance the additional amount for the GPL & NCAM project.

While it is difficult to predict whether or not we will have a surplus in 2024, the County currently has some significant favourable variances. Finance must go through our year end process, reconcile all accounts, complete adjusting entries and complete our annual audit. If there is a surplus in 2024 and/or 2025 those funds could be directed towards the unfinanced portion of the project and would reduce the amount needed from debt and/or reserves.

Assumptions and Estimates

It is important that Council understand the assumptions and estimates that are built into this report and its analysis.

The final projected cost for the GPL & NCAM project are not know with 100% certainty. The construction costs have been established through and agreement with the main contractor however, there are some costs that are still estimates:

- The furniture, fixtures, and equipment (FF&E) procurements are currently underway. This is a smaller part of the overall budget but since these are not all finalized the amounts in the projected costs are still estimates. There is a risk that some of these procurements may be negatively impacted by inflation since the project has taken longer than originally anticipated.
- The interest expense on construction financing assumes that the debenture will be finalized in June of 2025. If the IO debenture is finalized earlier, this should reduce the overall interest expense from the construction financing.
- The amount of non-recoverable HST expense is an estimate based on the overall project cost. The County is required to have an appraisal done of the building after it is completed and pay HST based on the appraised amount. This could be higher or lower than the estimate included in the total projected cost.

Financial Impact

The financial impact has been outlined in the Discussion/Options section.

Member Municipality Impacts

These decisions will not have a direct on the member municipalities but will have an impact on the 2025 and 2026 County budget and levy.

Conclusion / Outcomes

1. It is recommended that the Finance and Audit Committee recommend that Council direct staff to immediately start the process for finalizing the existing debenture with IO in the amount of \$96,770,321.

2. It is recommended that the Finance and Audit Committee identify the unfinanced portion of the GPL & NCAM project (\$16,596,025) for separate discussion during budget deliberations at the December 18, 2024 Council meeting.

Attachments

1. Report 2024-158 ATTACH 1 'GPL and NCAM Debt Sensitivity Analysis'
2. Report 2024-158 ATTACH 2 'County Reserve Summary'