



City of
Peterborough

To: Members of the General Committee

From: Richard Freymond
Commissioner of Corporate and Legislative Services

Meeting Date: November 12, 2019

Subject: Report CLSFS19-051
Investing Proceeds from Sale of Peterborough Distribution Inc.

Purpose

A report to seek Council direction with regard to investing the proceeds from the sale of Peterborough Distribution Inc. to Hydro One.

Recommendations

That Council approve the recommendations outlined in Report CLSFS19-051 dated November 12, 2019, of the Commissioner of Corporate and Legislative Services, as follows:

- a) That with respect to use of the proceeds as a result of the sale of Peterborough Distribution Inc., Council give preliminary endorsement to the establishment of a City of Peterborough Legacy Fund as described in Report CLSFS19-051 for purposes of information gathering and public consultation;
- b) That with respect to use of the proceeds as a result of the sale of Peterborough Distribution Inc., Council give preliminary endorsement to investing in renewable energy through the City of Peterborough Holdings Inc., and as described in Report CLSFS19-051 for purposes of information gathering and public consultation;
- c) That upon approval of recommendations a) and b), staff be directed to arrange presentations by representatives of both the ONE Investment group and CoPHI, at a future date; and,

- d) That staff be directed to provide a further report on the results of all information gathered, the public consultation process and final recommendations as to how the funds should be invested, and that the report be provided no later than March 2020.

Budget and Financial Implications

There are no budget and financial implications at this time.

The negotiated sale price of Peterborough Distribution Inc. to Hydro One is \$105 million. After fees and retirement of debt obligations, the net sale proceeds are expected to be in the range of \$50 to \$55 million.

Background

Council, at its meeting of December 15, 2016, approved the recommendations in Report CAO16-018, City of Peterborough Holdings Inc. Recommendation to City of Peterborough – PDI Divestment to Hydro One as follows:

- e) That the Net Proceeds of the sale be placed in an interest bearing reserve account under the control of the City Treasurer with details and options available to Council for investment of the funds to be reported to Council in the second quarter of 2017, including an option to reinvest the funds in City of Peterborough Holdings Inc. to support renewable power generation projects with an interest rate of at least 6% as a point to compare all other options.

The 2017 date was set before staff had a full appreciation of just how long the process was going to take for the completion of a transaction of this size.

Sale of PDI - Current Status

The Agreements between Hydro One, the City and PDI were signed on July 31, 2018. The sale transaction is subject to approval by the Ontario Energy Board (OEB). Hydro One submitted the application for approval to the OEB in October 2018 and the OEB issued a notice to the public regarding the sale on December 18, 2018. Approval has been delayed and is expected to occur in 2020. The closing of the sale transaction will occur within approximately 90 days of receipt of OEB approval.

In compliance with the Asset Purchase Agreement and the Transition Services Agreement, Peterborough Utilities Services Inc. has been reorganized and a new company has been created (Peterborough Services Corp) to separate out the electrical utilities operations (staff and assets) from the water and other operations in preparation for finalization of the sale transaction. There will be a transition period immediately after the financial close where the electrical business will be operated very much like it is now for Hydro One until a successful integration of the business into Hydro One's business.

To prepare for that, information systems, reporting and business proactive changes have been made or are occurring to meet the expected requirements from Hydro One.

Discussion

In accordance with the direction of the previous Council, and for purposes of discussion and public consultation, staff are putting forward two suggestions on how the net sale proceeds should be invested:

- 1) The creation of a City of Peterborough Legacy Fund, and
- 2) Investing in Renewable Energy.

Legacy Fund

The basic tenet of a legacy fund is the preservation of the capital in perpetuity. This means that only the investment income would be available to be spent on an annual basis.

Key features of a framework in support of a legacy fund idea would be:

- investing the funds to maximize returns with a minimum of risk to maintain and potentially grow the original proceeds. This strategy requires a portfolio composed of a mix of financial instruments with guaranteed returns which could be augmented by some higher risk instruments.
- Use of the income to be directed towards financing future capital works.
- Set a requirement for a 2/3 majority vote of Council to approve the spending of any of the capital.

In the normal course of City operations, staff are continuously managing a portfolio of short-term investments, as per the existing Investment Policy established by Council on October 24, 2016 through Report CPFS16-031. Depending on Council's direction with respect to establishing a Legacy Fund, amendments to the existing policy may be required, or a new policy created, to capture the intended purposes of the Legacy Fund.

Invest in Renewable Energy

The City of Peterborough has a proven track record in developing renewable energy through its investment company, City of Peterborough Holdings Inc. (CoPHI). CoPHI operates electricity and water distribution systems in the City and surrounding communities. The Company also develops and operates renewable hydro and solar generation facilities and operates a wholesale metering business. The Company and its related entities operate as the Peterborough Utilities Group.

As published in their 2018 Annual Report, the efforts of the Company over the past several years have provided a base for renewable energy equivalent to powering approximately 52% of the City's supply. The Company has been a conservation leader in providing its customers with opportunities to reduce their consumption.

Over the years, the investment returns paid to the City, as the sole shareholder, has been an important source of revenue and has been very effective in mitigating tax increases and moving important capital works forward.

For 2019, it is anticipated that the company will pay the City \$5.78 Million in dividends (2018: \$5.67 million), a 1.94% increase over the previous year. Cumulatively, at the end of 2019, \$90.75 million in distributions (dividends and interest) will have been paid to the City by the utility since its incorporation in 2000. The distributions to the City are funded by the operating companies of CoPHI. As stated in the 2018 Annual Report, due to the capital requirements and regulatory restrictions impacting cash flow in PDI, the majority of the distribution in 2018 was provided by the generation and other unregulated businesses.

From the City's perspective, the nature of the investment being proposed in this option would be in the form of common or preferred shares in CoPHI or any of its direct or indirect subsidiary companies. This is similar to today, whereby the City's current investment in CoPHI is in the form of common shares and supplemented by earnings retained in the company. A portion of the retained earnings are then reduced by the annual dividend payment to the City.

There are certain restrictions in the **Municipal Act, 2001** that would most likely preclude the investment being in the form of secured debt. That is, debt that is backed by the presence of collateral.

Comparing the Two Ideas

The two thoughts being put forward for consideration in this report are similar, yet different. The following observations compare the two ideas:

- Income from the Legacy Fund could be of immediate use and would most likely take the form of interest revenues, whereas investing in renewable energy should be considered a longer-term investment, the income from which would most likely be in the form of both interest and dividends payments.
- Although the basic tenet of a Legacy Fund is preservation of capital, investing in renewable energy would be a use of capital for that specific purpose.
- Financial returns from either scenario are almost impossible to predict and are dependent upon a myriad of factors, including interest rate fluctuations, risk tolerance, exposure to changes in the capital market, the term of the financial instrument, the timing of required use of cash, the overall financial success of the renewable energy project(s), etc.
- Both are being proposed as benefiting the City's capital program, without restricting the use to any one functional area. For instance, providing financial resources in response to the Declaration of a Climate Change Emergency, fits nicely within the concept of a Legacy Fund.
- At Council's discretion, the ONE Investment Group be considered the investment management firm to oversee the Legacy Fund Investments. From the perspective of renewable energy, oversight is already established in the form of the CoPHI Board of Director's.

- Approval of the utilization of cash from either form of investment, would be subject to Council approval through the annual budget process.

Community Consultation

Meaningful engagement with the community is central in considering how to invest the sale proceeds. Staff propose that subsequent to the presentations by ONE Investment Group and CoPHI to Council the City would use information from both presentations to create a survey, which would be available online and in hard copy, and to engage with advisory and stakeholder groups, including, but not limited to, the following:

- Housing Action Task Force
- Peterborough Environmental Advisory Committee
- Arts, Culture and Heritage Advisory Committee
- Arenas, Parks and Recreation Advisory Committee

Advisory and stakeholder groups beyond those listed above may be approached to seek their submissions.

The broader community consultation will largely be done through the survey and possibly additional online tools using the City's online community engagement platform, Connect Peterborough.

While the creation of a Legacy Fund to generate revenue for capital work or a new substantial investment in renewable energy generation would set a significant long-term direction for the community, both are broad concepts with specific details to follow, either through annual budget recommendations to Council for capital spending from a Legacy Fund or decisions by the CoPHI Board on renewable energy projects. Due to the high-level discussion, a community survey and specific stakeholder engagements are proposed for the consultation process.

Results from the consultation would be reported back to Council for its consideration when deciding how to proceed.

Next Steps

Staff envision the following as next steps to aid in deciding on how to use the sale proceeds:

- To the extent that Council is supportive of establishing a Legacy Fund, staff will reach out to ONE Investment with a view to arranging a presentation for Council. ONE Investment is a non-profit organization established in 1993 and formed by two key municipal associations, Municipal Finance Officers' Association (MFOA) and Association of Municipalities of Ontario (AMO), through its services arm, Local Authority Services (LAS). As part of their advisory services, ONE Investment provides customized investment advice and guidance for municipalities. They have provided advice to several municipalities who have recently sold their utility distribution companies, including Norfolk County, Town

of Midland and City of Woodstock. Based on their September 2019 Performance Report, ONE Investment manages approximately \$2.1 Billion in various portfolios on behalf of municipalities.

- To the extent that Council is supportive of investing in renewable energy, staff will work with senior management at CoPHI with a view to arranging a presentation to Council by the CoPHI Board that would further delineate what may be possible.
- Staff will solicit feedback from the community as described above with a view to updating Council on the results.

In the unlikely event that the funds are received prior to the end of March 2020, the monies will be placed in a short-term investment with CIBC, the City's financial institution, until the investment allocations have been approved.

Summary

This report provides a starting point for discussion about what to do with the proceeds of the sale of PDI. Both ideas being put forward have the potential to benefit the community for generations yet to come.

Submitted by,

Richard Freymond
Commissioner of Corporate and Legislative Services

Contact Name:

Richard Freymond
Commissioner of Corporate and
Legislative Services
Phone: 705-742-7777 Ext. 1863
Toll Free: 1-855-738-3755
Fax: 705-876-4607
E-mail: rfreymond@peterborough.ca