**Township of Scugog
Staff Report**

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**Report Number:** FIN-2024-039

**Prepared by:** Laura E. Barta, CPA, CMA, Director of Finance / Treasurer

**Department:** Finance

**Report To:** General Purpose and Administration Committee

**Date:**  October 8, 2024

**Reference:** Strategic Direction 2: Sustainability: Improve sustainability through financial management, innovative funding and efficient and effective delivery of services

SD2 Objective 1: Formalize long-term financial planning to enhance informed decision making

**Report Title:** **Response to Provincial ERO Posting on Surety Bonds**

## Recommendations:

1. **THAT** Report FIN-2024-039, Response to Provincial ERO Posting on Surety Bonds, be received; and
2. **THAT** Council direct staff to respond to the ERO posting.

## Background:

* 1. **Township’s Current Practice**

The Township of Scugog does not currently accept Surety Bonds as a form of security for development agreements. On November 27, 2023 Council approved report FIN-2023-034 that deferred the acceptance of Surety Bonds as an option for security in development agreements to the passing of the Provincial regulation that was proposed as part of Bill 109. While no regulation has yet been passed, the draft regulation is currently available on the Environmental Registry of Ontario (ERO) for review and comment.

* 1. **ERO Posting**

ERO number 019-9198, being a proposed regulation under section 70.3.1 of the Planning Act will enable the use of Pay-on-Demand Surety bonds to Secure Land-Use Planning obligations. This was posted on September 16, 2024 with the comment period ending on October 16, 2024 and reads as follows:

**Proposal details**

**Landowners/homebuilders often require municipal approvals to move forward with their development proposals, such as housing projects. When approving a development proposal, municipalities may impose conditions on the homebuilders, which could include obtaining financial assurance from the homebuilder that the required public infrastructure (e.g., roads, sidewalks) or improvements (e.g., plantings) are built as per municipal standards and function as intended. Typically, this financial assurance takes the form of a Letter of Credit (LOC) issued by a bank. If a homebuilder fails to fulfil their contractual obligations, the municipality can draw on the LOC to complete the work to its satisfaction.**

**Ontario has heard from stakeholders that instruments, such as LOCs, which municipalities generally require to secure homebuilder obligations when building communities, tie up the homebuilder’s capital that could otherwise be invested in additional home-building projects and make some projects that currently can’t obtain financing more viable.**

**A wider acceptance of pay-on-demand surety bonds is regarded by some homebuilders as a means to help free up funds for housing projects while providing municipalities with the necessary assurance that they would have ready access to funds, similar to a LOC, to fulfil any conditions that are not met by the homebuilder.**

**Under Bill 109, the *More Homes for Everyone Act, 2022,* the province amended the *Planning Act* to provide regulation-making authority to the Minister of Municipal Affairs and Housing to authorize landowners to stipulate the instruments to be used to secure municipal obligations that are conditions of land-use planning approvals. The Minister may prescribe the instruments that landowners and other applicants can choose from as well as the circumstances in which the authority can be exercised.**

**As part of Bill 185, the *Cutting Red Tape to Build More Homes Act, 2024,* the government announced that it would consult on a potential regulation to prescribe instruments, such as pay-on-demand surety bonds, to secure municipal obligations that are conditions of land-use planning approvals. A wider acceptance of pay-on-demand surety bonds is one of many targeted steps to support the increase of housing supply in Ontario.**

**The government is now proposing a regulation under section 70.3.1 of the *Planning Act*. The proposed regulation would authorize homebuilders to use a pay-on-demand surety bond with prescribed features to secure municipal obligations that are conditions of land-use planning approvals.**

**Pay-on-Demand Surety Bond**

**A pay-on-demand surety bond is a three-party instrument that involves obligations and rights of a principal (i.e., homebuilder), the obligee (i.e., municipality) and a surety i.e., the insurer).**

**The bond represents a promise by a surety (i.e., the insurer) to pay the oblige (i.e., municipality) an agreed amount, on demand, if the principal (i.e., home builder) fails to meet the agreed upon development obligation.**

**Proposed Mandatory Elements of a Pay-on-Demand Surety Bond**

**1. Licensing requirement**

**The pay-on-demand surety bond would be required to be issued by an insurer that is licensed under the *Insurance Act* to write surety insurance.**

**This would cover insurers that are licensed to write insurance in Ontario and that are overseen by the Financial Services Regulatory Authority of Ontario.**

**2. Credit Ratings requirement**

**In order to minimize credit risk to municipalities of the pay-on-demand bonds, the insurer would be required to meet one of the following credit ratings:**

* **Dominion Bond Rating Service as “A” or higher;**
* **by Fitch Ratings as “A-” or higher;**
* **by Moody’s Investors Service Inc. as “A3” or higher;**
* **by Standard and Poor’s as “A-” or higher;**
* **by A.M. Best Company, Inc. as “A” or higher.**

**This is an important feature to ensure that if a pay-on-demand surety bond is called on by a municipality, the surety’s assurance to pay the amount due and on time is supported by a third party (i.e., credit rating) assessment.**

**3. Guaranteed payment**

**The pay-on-demand surety bond issuer (i.e., insurer) guarantees payment to the
oblige (i.e., municipality) if the principal (i.e., homebuilder) defaults in performing the obligation guaranteed by the bond.**

**This feature requires the insurer to make payments to the municipality for amounts demanded by the municipality if the municipality determines, in its sole discretion, that the principal (i.e., homebuilder) has defaulted in performing the obligation guaranteed by the bond and provides written notice of the default to the principal (i.e., homebuilder) and the insurer.**

**4. Timely payment**

**The insurer would be required to make payment to the municipality within 15 business days of being provided with a written notice of default. This feature ensures that the municipality, in the case of default, would have timely access to funds so that it can remedy/complete the works required on the land.**

**5. Partial Drawdowns**

**The pay-on-demand bond instrument would provide for partial drawdowns. This means that, similar to a LOC, a municipality would release portions of the security (i.e., reduce the amount of the bond) when it is satisfied that the condition of development has been fulfilled by the homebuilder.**

**6. Cancellation**

**The insurer would be required to provide a written notice to the municipality and the principal (i.e., homebuilder) at least 90 days in advance of its intention to terminate the pay-on-demand surety bond.**

**The principal (i.e., homebuilder) would be required to provide the municipality with a replacement security (e.g., LOC, another equivalent pay-on-demand surety bond) within 60 days of the receipt of the notice. Failing which, the existing pay-on-demand surety bond would remain in full force.**

**The Ministry of Municipal Affairs and Housing is not proposing to enumerate the specific circumstances in which the authority can be used in regulation.**

**Analysis of Regulatory Impact**

**The province amended the *Planning Act* to provide regulation-making authority to the Minister of Municipal Affairs and Housing to authorize landowners to stipulate the instruments to be used to secure municipal obligations that are conditions of land-use planning approvals. The Minister may prescribe the instruments that landowners and other applicants can choose from as well as the circumstances in which the authority can be exercised.**

**The government is proposing a regulation under section 70.3.1 of the *Planning Act*. The proposed regulation does not require landowners and municipalities to use pay-on-demand surety bonds. However, if a landowner chooses to provide a pay-on-demand surety bond to secure municipal land-use planning obligations, then a municipality would be required to accept this instrument as a financial assurance with the instrument having certain mandatory features as set out in the proposed regulation.**

**There would be some financial and time costs related to learning about the regulation and drafting policies on pay-on-demand surety bonds. These costs are estimated to average $1,400 per municipality and would generally be incurred around the time a proposed regulation is introduced.**

## Discussion:

* 1. **General Concerns – Lack of Flexibility**

Staff have reviewed the proposed regulation and have some concerns with it as it currently stands. The concerns deal mainly with the lack of flexibility offered to municipalities. The use of these bonds is at the whim of the developer and does not permit the municipality to include any restrictions or limitations. As the draft regulation currently reads, there are no options for the Township to allow for unique circumstances. Basically, if the bonding company meets the requirements set out in the regulation, there is an obligation for the municipality to accept this form of payment for the full amount of the security required.

In reviewing other municipal policies and processes, many have imposed minimums and maximums for the dollar amounts that they are willing to accept. Pickering as an example will only take Surety Bonds up to a limit of $15 million. Amounts over that level would be required to be secured with a Letter of Credit. Ajax currently has a $2 million dollar limit. While the Township’s draft policy does not currently have limits, it may be prudent to impose them at some future date or on some types of development. As it stands, the current regulation would not allow the Township to impose any limits on the dollar values or any combination of Surety Bonds and Letters of Credit. In addition, the Township may wish to offer the option of using surety bonds for some planning agreements while only accepting LOC for other types of land use planning applications. If the regulation is approved as presented, no limits or restrictions will be allowed.

**2.2** **Review of Township’s Current Draft Policy**

The Township’s draft policy mirrors many of the requirements in the policy that was previously approved by the Region of Durham. The provincial draft regulation appears to have a similar theme however some areas are not clear in the regulation and could be problematic. These can be broken out in the following categories:

* + 1. **Credit Rating**

The Township’s draft policy addresses the requirements for the surety provider including credit rating agencies and levels that will be acceptable. The proposed regulation utilizes four of the same credit rating agencies, however it has added one that the Township’s draft policy does not currently recognize. Should the surety company reference an A.M. Best Company rating only, the municipality should have the right to reject it.

* + 1. **Longevity**

The Township’s draft policy also expects the surety bond provider to have been in this business for a period of 10 years and monitored by the office of the superintendent of Financial Institutions. This is seen as a way to measure their commitment to this line of business and their continued sustainability. The regulation does not include any measure of this commitment.

* + 1. **Irrevocable**

It is critical that any security provided to guarantee that the promised work will be completed in accordance with the Township’s requirements be irrevocable. Development agreements can be in place for many years and the security provided must be available until all the terms of the agreement have been satisfied. The proposed regulation does not mention anything about the bond being irrevocable. This is a major issue for municipalities and although the wording in the regulation speaks of cancellation, it fails to mention they need to be “irrevocable”.

* + 1. **Right to Refuse**

The regulation does not give the Township the right to refuse a surety bond for any reason. This could create issues for the Township if the surety provider places limitations on their bond. To protect the best interest of rate payers, the Township should have the right to refuse any surety bond that does not conform to the Township’s specifications.

* 1. **Cost and Training**

The last section of the ERO posting recognizes that there will be a financial cost related to learning about the regulation and drafting policies that should average $1,400. Staff are not sure how this amount was calculated and are not currently aware of any training or other resources that are currently available. The Township’s current delay in implementing the acceptance of surety bonds could be addressed by having the Province provide the details on companies licensed to provide surety insurance in Ontario and by providing detail of each companies credit worthiness on a regular bases. Having this information current and readily available from a trusted source would go a long way towards enabling acceptance for municipalities with limited staff resources.

The Township’s response to ERO number 019-9198 is shown in the attachment to this report.

## Financial Implications:

Providing a response to the ERO posting will not have a direct financial impact on the Township. Having the regulation approved as proposed will require the Township to accept surety bonds and will have cost implications related to monitoring. Staff are still working to develop processes to monitor the financial health of the surety providers, and this could involve some costs.

## Communication Considerations:

Staff will post the response on the ERO site.

## Conclusion:

That Council approve staff’s response to the ERO posting and direct staff to post it. If the regulation is approved by the Ministry, staff will report back to Council and bring forward an updated policy that incorporates the regulation requirements.

Respectfully Submitted by: Reviewed By:

Laura E. Barta, CPA. CMA Ralph Walton Director on Finance/Treasurer Acting CAO

## Attachments:

Attachment 1: Township of Scugog Response to ERO number 019-9198

Report Approval Details

| Document Title: | Response to Provincial ERO Posting on Surety Bonds - FIN-2024-039.docx |
| --- | --- |
| Attachments: | - Attachment 1 - Response to ERO Posting 019-9198.docx |
| Final Approval Date: | Oct 2, 2024 |

This report and all of its attachments were approved and signed as outlined below:



Ralph Walton