MUNICIPAL FINANCE OFFICERS' ASSOCIATION OF ONTARIO

Summer | 13

Municipal Act Review: Recommendations Strengthening Core Legislation

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Municipal Act Review

1. Executive Summary

MFOA's review of the *Municipal Act, 2001* ("the Act"*)*, makes numerous recommendations to improve the Act in support of municipal financial sustainability and independence, as well as other principles outlined in the report that guide MFOA's work.

This submission contains recommendations on revenue restrictions and expansion, financial administration and reporting, and building capacity to manage the province-wide infrastructure deficit. It also imagines a Municipal Act that encapsulates the full range of municipal legislation and regulations. The specific recommendations are summarized below.

Recommendation 1: That the proposed amendments for streamlining and clarifying various elements of tax administration be implemented for the 2014 tax year.

Recommendation 2: That Part IX of the Act is amended to give municipalities the authority to opt out of the provisions of tax capping.

Recommendation 3: That O. Reg 438/97, a regulation under Part XIII of the Act, is amended as set out in the CHUMS/LAS submission to the Debt and Investment Committee.

Recommendation 4: That O. Reg 284/09, a regulation under the Act, is retained in its current form.

Recommendation 5: That the current "Heads and Beds" rate of $75 be raised to $183 beginning in 2014 and reset every 5 years with each review of the Act.

Recommendation 6: The Province should issue regulations under subsection 40(3) of the Act, 2001 to permit municipalities to designate, operate and maintain toll roads.

Recommendation 7: The Province should issue regulations to permit the sale of debt as provided in section 305.

Recommendation 8: Amend the Act to include a broad power to impose taxes beyond the property tax as is found in section 267 of the *City of Toronto Act, 2006*, to be determined by a provincial revenue consultation process. The power to impose non-traditional taxes must also include any ancillary enforcement powers as well as powers to impose fines and penalties in cases of non-compliance.

Recommendation 9: In 2014, the Province and municipal sector should begin discussions on a comprehensive strategy to address infrastructure gaps in Ontario municipalities and to create investment strategies that compliment and support long-term financial planning in the sector.

Recommendation 10: Regulations and legislation that have a significant impact on municipal finances should be brought under the umbrella of the Municipal Act regulations and legislation.

3. Introduction

This review of the Act has been prepared by the Municipal Finance Officers' Association of Ontario (MFOA). The Municipal Finance Officers' Association (MFOA) was established in 1989 to represent the interests of Municipal Finance Officers across Ontario. MFOA promotes the interests of its members in carrying out their statutory and other financial responsibilities by initiating studies and sponsoring seminars to review, discuss and develop positions on important policy and financial management issues.

4. Rationale

Subsection 3(2) of the Act states that:

> The Ministry of Municipal Affairs and Housing shall initiate a review of this Act before the end of 2007 and thereafter within five years of the end of the previous review.

2012 was a Municipal Act review year and elements of the review have continued into 2013, therefore it is an opportune time for MFOA and its members to positively influence the Act.

5. Principles

MFOA believes that all good public policy should be principle based. Here are the principles that guide our specific recommendations for reform:

- **Financial sustainability:** Municipalities should demonstrate their status as independent governments in financial terms and strive to reduce dependence on external funding.
- **Modernization of the revenue framework:** Municipalities' own source revenues should be capable of directly reflecting the economic activities that take place within a municipality's borders. All groups using or benefiting from municipal services should contribute to the provision of those services through municipal rates.
- **Strong financial management:** Prudent financial management practices and strong internal controls should be employed by municipalities.
- **Mutual respect:** We insist on a mutually respectful relationship between the municipal and provincial spheres of government.
- **Meaningful consultation and responsiveness:** Municipalities require meaningful consultation on provincially initiated policy changes, commensurate resources to implement provincially initiated changes and responsive legislative and regulatory measures in areas of widespread municipal concern.

6. Tax Administration

MFOA members have identified three amendments that should be made to the sections of the Act dealing with municipal taxation and tax capping. These proposed amendments have strong consensus in the sector and the support of MFOA and OMTRA. The proposals, intended to correct administrative issues or to provide greater clarity, would make significant improvements in the area of tax administration. These are summarized in Appendix A at the end of this document.

Recommendation 1: That the proposed amendments for streamlining and clarifying various elements of tax administration be implemented for the 2014 tax year (Appendix A).

7. Tax Capping

Part IX of the Act deals with capping of taxes for the commercial, industrial and multi-residential property tax classes. Since capping was introduced in the late 1990s, a number of measures have been introduced to give municipalities greater flexibility to accelerate the process of moving properties towards full Current Value Assessment taxation. As a result of these measures, many municipalities now have relatively few properties where taxes are capped. In addition, tax protection in the form of assessment phase-in also applies to the commercial, industrial and multi-residential classes. Therefore, it is prudent to amend the Act to provide municipalities with the ability to opt out of the tax capping provisions of the Act.

MFOA supports the paper prepared on this topic by Municipal Tax Equity, which is attached in Appendix B.

Recommendation 2: That Part IX of the Act is amended to give municipalities the authority to opt out of the provisions of tax capping (Appendix B).

8. Investment Powers

Part XIII of the Act deals with debt and investment. MFOA has a keen interest in municipal investment powers since it provides investment pooling services to the sector in partnership with the Association of Municipalities of Ontario (AMO), Matters related to debt and investment are routinely dealt with at the Debt and Investment Committee which is a committee representing municipalities, associations, investment dealers, rating agencies and several provincial ministries.[1]

MFOA, AMO, and other municipal members, submitted a number of proposals to the Debt and Investment Committee for amending the regulation dealing with O. Reg. 438/97 Eligible Investments and Related Financial Agreements. Our position paper is set out in Appendix C.

[1] The ONE Investment program is an investment pool run jointly by the CHUMS Financing Corporation (a subsidiary of the MFOA) and LAS (a subsidiary of AMO).

Recommendation 3: That O. Reg 438/97, a regulation under Part XIII of the Municipal Act, be amended as set out in the CHUMS/LAS submission to the Debt and Investment Committee (Appendix C).

9. Budgeting for Expenses

Section 294.1 of the Act requires municipalities to prepare financial statements each year in accordance with "generally accepted accounting principles" established by the Public Sector Accounting Board of the Canadian Institute of Chartered Accountants. In 2010, municipalities prepared financial statements for 2009 that required tangible capital asset accounting for the first time. This represents a significant change in municipal accounting practices.

O. Reg 284/09 – Budget Matters came into force on January 1, 2009 and complemented the new requirement for municipalities to report on their tangible capital assets and move from modified accrual to full accrual accounting in their audited financial statements. The intent of the regulation was not to change the way municipalities budget, but to draw Councils' attention to specific significant 'accrual' expenses.

Accordingly, under the regulation municipalities may exclude amortization costs, post-employment benefits expenses, and solid waste landfill closure and post-closure expenses when preparing annual budgets. The regulation requires councils to adopt annual reports that show the impact of not fully covering the estimated costs of these expenses.

The MFOA supports O. Reg. 284/09 as it is currently written. The status quo respects municipal autonomy, while presenting the financial position of the municipality and linking the budget document to the greater financial management framework. Our Board approved position paper can be found in Appendix D.

Recommendation 4: That O. Reg 284/09, a regulation under the Municipal Act, is retained in its current form (Appendix D).

10. Existing Municipal Revenue Sources

Several sections in the Act have never had regulations to give them force. These include:

- Section 323: "Heads and Beds"
- Section 40: Toll roads
- Section 305: Sale of debt

Section 323: Heads and Beds

A number of properties in Ontario are subject to taxation, but not based on current value assessment. These properties, which are identified in section 323 of the Act, include:

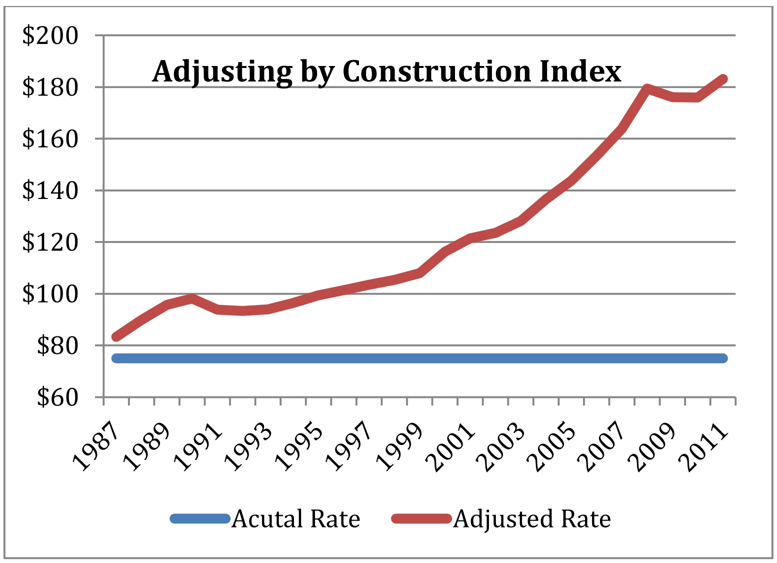
- Colleges and universities
- Public hospitals or provincial mental health facilities
- Correctional institutions, and

- Residences for the developmentally disabled

For these types of properties the tax is determined by applying a regulated rate against the number of students (universities, colleges) or beds (correctional facilities, residences for the developmentally disabled). Subsection 323(10) gives the Minister of Finance the authority to establish the applicable rate by regulation.

Currently the rate is set at $75. This rate was established in 1987 and has not been adjusted in the subsequent 25 year period. MFOA has previously recommended that this rate be adjusted to reflect inflation over the period. Others have also recommended such changes.

Based on the non-residential construction index, the rate should be approximately $183 when adjusted for the index's inflation.



Recommendation 5: That the current "Heads and Beds" rate of $75 be raised to $183 beginning in 2014 and reset every 5 years with each review of the Municipal Act, reflecting inflation in the non-residential construction index.

Section 40: Toll Roads

Subsection 40(1) of the *Municipal Act, 2001*, states that:

> **40.** (1) A municipality may,
> (a) designate a highway as a toll highway; and
> (b) operate and maintain the designated highway as a toll highway.

Notwithstanding this grant of power, Subsection 40(2) states that "a municipality does not have the power to designate, operate and maintain a highway as a toll highway until a regulation is made under this section." Subsection 40(3) provides for broad regulation authority for the Lieutenant Governor in Council.

This provision has been in the Act for over 10 years. It would be prudent to formulate regulations that will enable municipalities to designate or operate toll roads if they deem it necessary.

Recommendation 6: The Province should issue regulations under subsection 40(3) of the Municipal Act, 2001 to permit municipalities to designate, operate and maintain toll roads.

Section 305: Sale of Debt

Subsection 305(1) of the Act states that:

> **305.** (1) A municipality may sell any prescribed debt payable to the municipality to any other person in accordance with the prescribed rules and conditions. 2001, c. 25, s. 305 (1); 2002, c. 17, Sched. A, s. 48 (1).

Subsection 305(2) grants the Minister of Municipal Affairs and Housing the power to issue regulations to prescribe the types of debt for the purposes of section 305. To date, no regulations have been issued, therefore we recommend that regulations be issued to make this part of the Act come into force.

Recommendation 7: The Province should issue regulations to permit the sale of debt as provided in section 305.

11. New Revenues

The Need

Municipalities of all sizes face significant financial pressures. Financial pressures with respect to growth related capital costs, infrastructure backlogs, escalations in the costs of capital projects and higher standards for services coming from citizens and/or government regulations necessitate a comprehensive review of alternative own source revenues for municipalities that go beyond the provisions currently found in the City of Toronto Act, 2006. In addition, by the end of 2013, work on asset management plans will yield valuable information about the size and nature of the infrastructure gap in Ontario municipalities. As we move into 2014, addressing these realities requires a multi-pronged solution that includes, at the very least:

- Long-term sustainable funding for all municipalities, but particularly those with a limited ability to raise own source funds, and
- New revenue sources for municipalities, based on a provincial revenue consultation process
- Ancillary enforcement powers in cases of non-compliance with non-traditional taxes

Part X of the City of Toronto Act, 2006, authorizes the City to impose taxes. Subsection 267(1) states that:

> The City may, by by-law, impose a tax in the City if the tax is a direct tax, if the by-law satisfies the criteria described in subsection (3) and if such other conditions as may be prescribed are also satisfied. 2006, c. 11, Sched. A, s. 267 (1).

Many of our members have expressed a strong interest in alternative revenue sources. A recent report from Mississauga estimates that the land transfer tax alone could raise approximately $74 million annually, which would make a positive contribution to closing the City's infrastructure gap.

Recommendation 8: Amend the *Municipal Act, 2001*, to include a broad power to impose taxes beyond the property tax as is found in section 267 of the *City of Toronto Act, 2006*, to be determined by a provincial revenue consultation process. The power to impose non-traditional taxes must also include any ancillary enforcement powers as well as powers to impose fines and penalties in cases of non-compliance.

While MFOA has not endorsed any specific tools, it looks forward to progress on the revenue front. Municipalities will require new revenue tools to invest in future infrastructure and **these tools should not be limited to the GTHA**.

12. Financing Municipal Infrastructure

In 2001 the biggest additions to the Act were broad spheres of jurisdictional and natural person powers. These principles do not apply to financial sections of the Act and its regulations. This is contradictory, since municipal potential for responsibility and scope has increased without the corresponding tools to implement and finance this responsibility and scope.

In 2014 most municipalities will have asset management plans, which will identify gaps and needs. The provincial government should use this opportunity to launch a review process to understand the municipal infrastructure deficit, cost efficiencies, and new revenue tools specifically earmarked for infrastructure, focusing on dedicated tools for capital.

Recommendation 9: In 2014, the Province and municipal sector should begin discussions on a comprehensive strategy to address infrastructure gaps in Ontario municipalities and to create investment strategies that compliment and support long-term financial planning in the sector.

13. Regulatory Consistency

A significant amount of regulations and legislation that impact municipal finances are located outside of the Act. To ensure regular review of these regulations and legislation, and to ensure consistency between the principles used to govern municipal-provincial relations (municipal responsibility, independence, and accountability), regulations and legislation that have a high impact on municipal finances should be brought under the umbrella of the Act.

Recommendation 10: Regulations and legislation that have a significant impact on municipal finances should be brought under the umbrella of the Municipal Act regulations and legislation.

We would be happy to support MMAH in this legislative exercise.

14. Conclusion

MFOA has specified recommendations with respect to the following areas of the Act:

- Tax administration
- Tax capping
- Investment powers
- Budgeting for expenses
- "Heads and Beds" taxation
- Toll roads
- Sale of debt
- New revenue sources
- Financing municipal infrastructure
- Regulatory consistency

In addition, MFOA supports a broad review of revenue sources that should include, but not be limited to, financing transport services. Municipalities are moving to long-term financial planning and asset management, therefore we support a review of new revenue sources for all municipalities as well a general review of provincial transfer programs and processes to ensure that provincial transfers are made in a way that supports provincial objectives for long-term financial planning and municipal asset management.

Appendix A: Proposed Tax Administration Amendments

Dear Ken and the Executive of the AMTCO/OMTRA,

In response to your request for suggested amendments to the *Municipal Act, 2001* (MA), we have encountered several issues with the act as it now stands pertaining to tax sales that we think could use another look. We have outlined three problems below along with suggestions to address the issues. We have a fourth issue that we are still discussing for possible suggestions, however we are forwarding on the problem to you in the meanwhile for consideration for possible suggestions for resolution.

ISSUE NO. 1
Surplus Funds that are required to be paid into court following a readvertised tax sale conducted in accordance with MA section 380.1

Problem
As the wording of the act stands now, all surplus funds after a tax sale must be paid into court pursuant to MA section 380(2) with surplus funds described in section 380(2) as the proceeds of the sale, minus the cancellation price. Tax sales are most often unsuccessful when the amount of taxes owing (for some reason or another) overwhelms the value of the property. In situations where the municipality has written off taxes following a prior unsuccessful sale per s. 354 and has readvertised the property for sale per s. 380.1 at a new lower cancellation price comprised of the remaining taxes and costs, the surplus funds from the successful readvertised sale are required by s. 380(2) to be paid into court where the delinquent owner or some other party with an interest in the property could claim them. It only seems fair that if the municipality has written off taxes and is lucky enough to have a tender in a readvertised sale for more than the new cancellation price, that they should be able to apply those proceeds to the taxes that were written off.

Suggestion:
The *Municipal Act 2001* be amended so that if there are surplus funds after a readvertised sale where the municipality has written off taxes and reduced the cancellation price from the first sale as provided by MA sections 354 and 380.1, the surplus funds should be applied to the cancellation price for the re-advertised sale *and then to the amounts that were written off* before any balance is paid into court.

ISSUE NO. 2
An error in paragraph 3 of Form 10 Final Notice of Readvertisement. It appears to offer an option for an extension agreement in paragraph 3 that would be in contravention of s. 378(1)

Problem
The window for entering into an extension agreement only exists for one year from the date the tax arrears certificate was registered as per MA section 378(1). The one year has passed before the property is advertised for the first sale date. It appears that the contents of the Form 3 Final Notice were copied into the Form 10 without consideration that the option of an extension agreement in paragraph 3 was not applicable to a readvertised sale.

Suggestion:
Reference to an extension agreement be removed from paragraph 3 in Form 10.

ISSUE NO. 3
Method of Payment Problem
Rule 25 states:

> Subject to clause (6) (1) (b), any payment required by this Regulation to be made in cash may be made by way of cash or money order or by way of bank draft or cheque certified by a bank or trust corporation.

This creates problems, and a potential lawsuit, when a certified cheque from a credit union is received.

It's important to note that in many communities, there is no bank or trust corporation; only a credit union. The nearest bank or trust corporation may be a hundred or more kilometres away. This makes it difficult for some potential tenderers or bidders to get a bank draft or certified cheque from a bank or trust corporation.

Suggestion:
Clause (6) (1) (b) of The Municipal Tax Sale Rules be amended so that it recites:

> accompanied by a deposit of at least 20 per cent of the tender amount, which deposit shall be made by way of money order or by way of bank draft or cheque certified by a bank or trust corporation or credit union or caisses populaires.

Rule 25 be amended so that it recites:

> Subject to clause (6) (1) (b), any payment required by this Regulation to be made in cash may be made by way of cash or money order or by way of bank draft or cheque certified by a bank or trust corporation or credit union or caisses populaires.

ISSUE NO. 4
Stalemate that occurs property when purchaser has paid balance owing pursuant to *Municipal Tax Sale Rules O. Reg 181/03* (Tax Sale Rules) 11(2), 12(2) or 16 and has been declared the successful purchaser, but refuses to sign the documents required to register tax deed

Problem:
We have encountered several situations where purchasers in a tax sale *pay their balance in full* as required in section 11, 12 or 16 of the Tax Sale Rules but then refuse to sign the Acknowledgement and Direction required for electronic registration or the Land Transfer Tax Affidavit required for paper registration. The treasurer is caught between various sections of the *Municipal Act 2001*. (MA) The "Successful Purchaser" has been declared in accordance with the above sections and MA Section 379(5) (a) says the treasurer

> … shall prepare and register a tax deed in the name of the successful purchaser or in such name as the successful purchaser may direct.

The treasurer is required to register the tax deed but does not have control over the purchaser signing the Acknowledgement and Direction required to register electronically or the Affidavit of

Land Transfer Tax required to register the paper document. Also, neither the Form 7 Tender, nor the Auctioneer's receipt contains enough information to draft a registerable tax deed under the current Land Registration Reform Act requirements, most particularly the birth date and chosen tenancy of the purchaser(s).

The municipality cannot go to the lower bidders in an auction as the auction is over at this point and everyone has gone. In a tax sale by tender, the tenders of everyone other than the "Successful Purchaser" have been returned. There is no provision to cancel only the sale portion of a tax registration and readvertise once the successful purchaser has been declared. The 90-day provision in section 22 of the Tax Sale Rules does not apply to this situation as this is to be used if completing the sale "would be unfair to the bidders or tenderers" and by the time it is discovered the Purchaser won't sign, the 90 day period is too short to accommodate a readvertised sale. Even if it did, it would totally undermine the tax sale process as purchasers could delay the cost and time of investigating a property until they are declared the successful purchaser, hold off on finalizing the registration until they complete their investigations and then get their money back if they decide they are unhappy with the deal. The municipality would be stuck with the cost of doing the whole sale over, with no confidence that the same thing wouldn't happen the next time around.

Another suggestion of declaring that there was no successful purchaser and then vesting would be patently unfair to the lower tenderers who submitted their tenders in good faith and particularly to the second highest tenderer who would have been the successful purchaser if the highest tenderer had not bid or tendered for a property he or she did not want.

This situation has arisen several times when it is obvious the bid or tender was submitted without the purchaser investigating matters such as crown interests, contamination and/or road access. They paid their balance so that lower bids or tenders are rejected and then went to check out the property to discover it is not the deal they were hoping for. They then demanded their money back and refused to sign the documents required for registration.

Note that the Prescribed Form 6 Tax Sale ad says:

> Except as follows, the municipality makes no representation regarding the title to or any other matters relating to the land(s) to be sold. Responsibility for ascertaining these matters rests with the potential purchasers.

When the purchaser refuses to sign the documents required for registration, how does the treasurer move forward with the property? The *Cunningham v. Front of Yonge* case confirmed that the tax sale is not final until the tax deed or notice of vesting is registered as per MA section 383(1). The ownership is still in the name of the old owner. What happens to the funds in this stalemate? They cannot be paid into court because the sale is not final yet as determined in the Cunningham case. If they are applied to the arrears, the old delinquent owner would retain ownership with the taxes all paid up at the expense of the purchaser. Could the purchaser come along years after the sale and demand their tax deed finally be registered?

Allowing purchasers to back out of a tax sale because they have not done their due diligence or they have simply changed their mind, undermines the whole tax sale process and results in added costs and time to the municipality, as well as tying up the title of the property.

It is apparent from the wording of the legislation that it was drafted at a time when no further action was required on the part of the purchaser in order to register the tax deed. The money was paid and the tax deed registered. With amendments to the Land Transfer Tax Act requiring that the affidavit can only be signed by the transferee (purchaser) and the Land Registration Reform Act providing for electronic registration, the sections of the Municipal Act that pertain to registration of the tax deed need to be updated to accommodate these changes.

In most cases, the properties are small and not worth much, so the purchaser is content to walk away or play a game of chicken to see if the treasurer will cancel the tax registration so the municipality can move on. The property may have a small assessed value, but this stalemate can cost a lot of money and time for the municipality.

At Realtax, we are still discussing several options for amendments to the Municipal Act, 2001 that would allow the treasurer to move ahead with these properties without getting caught up in a cumbersome legal quagmire. We thought, however, we would pass this issue along to you for your consideration in the meanwhile.

If you have any questions regarding this letter, please do not hesitate to contact us. We are pleased to offer any ongoing support we can.

Best regards,

Mary

RealTax Inc.

Mary MacCallum
Tax Sale Specialist
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Appendix B: Discussion Paper: Allowing Municipalities to Opt Out of Business Tax Capping

Discussion Paper

Allowing Municipalities to Opt Out of Business Tax Capping

Prepared by:

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Disclaimer and Caution

The information, views, data and discussions in this document and related material are provided for general reference purposes only.

Regulatory and statutory references are, in many instances, not directly quoted excerpts and the reader should refer to the relevant provisions of the legislation and regulations for complete information.

The discussion and commentary contained in this report do not constitute legal advice or the provision of legal services as defined by the Law Society Act, any other Act, or Regulation. If legal advice is required or if legal rights are, or may be an issue, the reader must obtain an independent legal opinion.

Decisions should not be made in the sole consideration of or reliance on the information and discussions contained in this report. It is the responsibility of each individual in either of a decision-making or advisory capacity to acquire all relevant and pertinent information required to make an informed and appropriate decision with regards to any matter under consideration concerning municipal finance issues.

MTE is not responsible to the municipality, nor to any other party for damages arising based on incorrect data or due to the misuse of the information contained in this study, including without limitation, any related, indirect, special or consequential damages.

Introduction and Purpose

Leading into 1998, sweeping reforms to the property assessment and taxation system were introduced by the Harris Government under the auspices of a number of key goals. Primary among these was ensuring that the assessment of real property and taxation practices across Ontario would be more fair, consistent, and understandable for taxpayers. Despite this original conviction, when faced with widespread criticism of their initial efforts the Government of the day quickly introduced a mandatory tax capping program for business class properties for the 1998 through 2000 tax cycles, which became known as the 10-5-5, in a laudable attempt to ease the transition to the new property tax regime.

Since these early days of reform, a variety of modified tax capping protection regimes have been implemented, replacing earlier successors with more permanent forms of relief. This tradition has created a long legacy of inequity within the multi-residential, commercial and industrial tax classes, which has effectively undermined the original goals of a stable, fair, transparent, and easily administered assessment and property tax system in the Province of Ontario.

Since the initial implementation of business tax capping in Ontario, Municipal Tax Equity (MTE) Consultants Inc. has worked intently with property tax professionals and municipalities across the Province to meet the policy and administrative challenges of these demanding and complicated tax protection programs. Our involvement with capping has ranged from the development of critical educational materials and seminars, to the provision of ad-hoc expert assistance, to the development and management of our full service stand-alone capping program.

To ensure that our clients and the municipal community at large have had access to the most current and highest quality information and support, MTE has invested the time and resources required at every stage to ensure that our capping expertise evolved in-step with the program itself. This evolution has been deliberate in terms of capping program and calculation mechanics, the options available to municipalities, and the changing patterns of capping outcomes.

From our unique vantage point over the capping landscape, we have been able to observe the history of capping unfold and have experienced its evolution at every stage. What has become particularly evident since the advent of CVA exclusion options in 2009 is that currently in many jurisdictions the actual impact of capping on the taxpayers' final liabilities has become marginal or non-existent. The capping program has diminished dramatically in importance, and is proving to have a material impact on fewer properties each year. The concern remains, however, that despite the limited number and magnitude of capping adjustments now being applied, the program as a whole continues to require significant time and resources to administer and manage.

In light of the fact that so many municipal councils have adopted policy schemes aimed at minimizing the impact of capping to the greatest degree possible, it seems obvious that the next change to Ontario's capping policy, as currently set out under Part IX of the Municipal Act, 2001, is for the Province to give municipalities the ability to Opt Out of the program in its entirety. Further, it may also be argued that 2013 is the most appropriate and opportune time for this change to be made.

The following discussion has been prepared to explore this issue in a systematic fashion. We at MTE hope that it will ultimately serve to crystallize, summarize and articulate the municipal perspective. To this end, we would ask that our clients consider the points, comments and general themes set out below, and provide us with any comment, thoughts and reactions that you may have.

Overview of Business Tax Capping

Legislation creating the mandatory "10-5-5" tax capping program was originally presented as a transitional measure to provide temporary tax protection for the 1998 through 2000 tax cycles. In 2001, however, the Province introduced additional property tax reforms that served to reinforce the prescriptive nature of the property tax policy environment in Ontario. At this time, tax capping became a permanent feature of the property tax landscape as the original, temporary 10-5-5 program was replaced on a Province-wide basis with a modified model known as the "5% limit on increases".

In response to concerns about the mechanics and prescriptive nature of the business tax capping program, the McGuinty Government announced a series of reforms for 2005 and subsequent taxation years. These reforms introduced a number of capping options to be used at the discretion of single and upper-tier municipalities. The initial range of optional tools included: 1) the ability to increase the annual cap from 5% of the previous year's final capped taxes up to 10%; 2) setting a second limit for annual increases of up to 5% of the previous year's annualized CVA taxes; and/or 3) the establishment of dollar thresholds of up to $250 whereby properties with nominal capping adjustments could be moved directly to their CVA tax liability in any given year. The 2005 reform package attempted to balance the interests of those in favour of maintaining property tax capping against the call to give municipalities the flexibility to accelerate movement towards full CVA taxation for all classes of property where this was the local preference.

The 2009 taxation year represented another in a long series of reform and reassessment cycles. In addition to a number of fundamental changes to the assessment system, which included the introduction of a four-year reassessment cycle coupled with a program to phase-in assessment increases, the Province gave municipalities the option to begin permanently excluding individual properties from capping by utilizing "stay at CVA tax" and "cross-over CVA tax" tools.

Challenges at the Municipal Level

Municipalities throughout the Province have devoted significant resources to ensure compliant and appropriate implementation of the mandatory tax capping program since its inception. The capping program has proven to be an administrative and budgetary burden because of the increased complexity it has added to the annual tax billing exercise and the management of any in-year tax adjustments required in response to assessment appeals, tax rebates or other events that demand that taxes be recalculated.

Despite the burdens posed by the business tax capping regime, Ontario's municipalities have accepted the associated challenges and have demonstrated a high degree of local responsibility with respect to the shape and outcomes of this program as it applies to taxpayers. Since the original introduction of optional capping tools in 2005, municipal staff and decision makers have in the vast majority of cases shown a keen interest and willingness to capitalize on the various options provided by the Province in order to optimize local capping regimes and accelerate the greatest number of properties to their full CVA tax liability.

In addition to the application of the core capping calculation options, municipalities have widely utilized the “new construction” constraint options, which ensures new or significantly improved capped class properties are subject to CVA tax.

Based on our observations, the majority of municipalities across the Province have strategically and deliberately employed the mix of optional capping tools in each taxation year that proved to be the most effective in meeting their local capping objectives. For most, this has meant a marked decrease in the annual cost of capping protection being provided and a striking increase in the number of properties being taxed at their full CVA tax level (i.e. CVA multiplied by Applicable Tax Rates). This not only means that more tax bills are being issued without capping adjustments, it also means that when in-year adjustments are required, the end tax adjustment is most likely to be made in direct proportion to any change in assessed value. This is not the case for properties subject to either a cap or claw-back adjustment.

Case for Capping “Opt-Out” Policy

The increasing range of capping options provided by the Province since 2005 has been a welcome change from the more prescriptive environment, which characterized 2004 and previous years. Notwithstanding the current flexibility offered to municipalities to tailor their local capping programs, we believe that there is a significant consensus within the municipal community that it is time for municipalities to be given the ability to opt out of business tax capping entirely.

The McGuinty Government has proven it values policies that place the responsibility for local property tax decisions with the level of government most directly responsible for levying the tax itself. The Government’s policy changes surrounding capping options, tax ratio movement, and levy restriction rules (hard-capping), have all provided municipalities with greater autonomy to craft local tax regimes that truly reflect local priorities and objectives within a common set of Province-wide standards and criteria. The Government must now show its commitment to this trajectory, thereby making decisions with respect to the future of capping in our communities local responsibilities.

It should also be noted that the case for giving municipalities the ability to opt out of business tax capping is based on factors that go far beyond the argument for local autonomy; it is also strongly rooted in the fact that this specific program is outdated, redundant, inherently inequitable, administratively cumbersome and confusing to the taxpayer. The most relevant and critical of the concerns and issues raised by this program are explored below. In sum, it is MTE`s view that they create an overwhelming argument for the Government to make the continuation of capping a local choice.

Capping has been made Redundant by the Four-Year Phase-In Program

In its original incarnation, the tax capping program was introduced as a means to provide business tax payers with temporary relief as they became acclimated to the Province's new property tax and assessment system. In subsequent years, however, the protection provided to taxpayers has been less related to the original impacts of reform and more so due to the ongoing impacts of subsequent assessment base updates. While prior arguments could suggest that its continuation was necessary so as not to remove or deny protection, this program must now be seen as a redundant measure in light of the Province's successful four-year assessment phase-in program, which more effectively and equitably addresses assessment increases for all properties.

Capping Creates Inequitable Tax Treatment

One of the central tenets of Ontario's property assessment and taxation system is that all properties are subject to a uniform valuation date, and that similar properties are to be assessed in a similar manner across the entire Province. While tax rates do fluctuate by jurisdiction and property class, the overall structure of the system is intended to ensure that properties that are similar in nature, value and use carry a similar portion of the overall tax burden. The marked exception from this goal is the mandatory tax capping program for business class properties.

Under this system, two properties in the same municipality, assessed at the same value, can be subject to very different tax liabilities. While one may enjoy a large capping credit, the other could be forced to fund the cap with a tax liability in excess of what its CVA and prevailing tax rates would otherwise suggest. In another instance, one property may be eligible for capping protection going into the 2013 reassessment, while another, with the same 2012 and 2013 assessment might be excluded. There are endless combinations and examples that could be provided, but the critical point is that the capping program creates inequities by distorting the tax liability of each property subject to an adjustment, which results in similar properties paying disparate taxes. Ultimately, this undermines the intention of the property tax system to treat similar properties in a similar manner by breaking the link between one's assessment, the tax rates and the final taxes owing.

Capping also creates more subjective and global inequities in our property tax system. For example, in many jurisdictions, we see that the capping protection that is still being provided is concentrated to the benefit of a very few taxpayers. Those still captured by the capping rules are generally the very small minority, and it can be easily argued that it is unfair and inappropriate for a large number of business owners to be funding special treatment for a small sub-set of taxpayers. It should also be noted that in jurisdictions where the application of the claw-back option is not possible, or is insufficient to cover the costs of capping, the costs of protection for these small groups of business taxpayers must be funded by all other taxpayers. This concern is further amplified by the fact that the current system is designed to ensure that those receiving the greatest protection will continue to benefit with no specific end in sight.

Capping is Administratively Cumbersome and Complex

There are also a number of practical considerations beyond the program's utility that remain relevant regardless of how many or how few capping adjustments, if any, are required in any given jurisdiction. The capping program has proven to be very time-consuming, cumbersome and costly to administer. Simply undertaking the calculations, applying adjustments to specific properties and managing affected tax accounts requires an abundance of internal resources. Municipalities continue to devote considerable human and budgetary resources each year to ensure that tax bills and adjustments are accurate, compliant and timely; these resources could be more effectively and strategically deployed to other more productive ends if not for the demands of capping.

Once adjusted bills are issued, the complicated and intricate nature of the capping calculations themselves make them very difficult for the lay person, business owner, and even many tax professionals to understand. This coupled with the often counter-intuitive outcomes revealed on tax bills and tax adjustments, result in an ongoing demand for explanations from taxpayers and their agents.

This confusion and the awkwardness of the calculations has also had an impact beyond just the taxpayer. The Municipal Property Assessment Corporation (MPAC), the Assessment Review Board (ARB), and even Provincial courts have struggled with the capping implications of decisions and adjustments since the inception of the original program. Again, this confusion is often confounded by the potential for counter-intuitive results. For example, it is not uncommon for a property owner to spend time and money seeking a reduction in their assessment only to find out later that the reduction does not result in any change to their final "capped" tax liability.

For municipalities, this all means that intensive resources must be dedicated to the on-going management and maintenance of the capping program; for the taxpayer it often appears that their tax liability is arbitrary and incomprehensible.

Next Steps and Weighing In

2012 represents the fifteenth taxation cycle that has been impacted by mandatory tax capping in Ontario. It is MTE`s view that in light of the more effective, equitable and predictable protection provided by the ongoing assessment phase-in program, it is timely for an exit strategy option to be put in place. MTE is also of the opinion that it would be ideal to make this option available in conjunction with the next general reassessment. This would allow municipalities to carefully consider and evaluate the tax impacts and shifts associated with the 2013 reassessment campaign both with and without capping in place. Such insight would allow interested municipalities to make informed decisions about whether or not to continue with this form of tax protection into the future.

To provide municipalities with the flexibility needed to address their current priorities and circumstances with respect to mandatory tax capping protection, it is strongly recommended that the Minister of Finance and the Province of Ontario be requested to amend the contents of the Municipal Act, 2001 to allow upper and single-tier municipalities to opt out of the business tax capping program set out in Part IX of that Act for the 2013 taxation year and future tax cycles.

Appendix C: Recommendations Dealing with Municipal Investment Powers

THE One INVESTMENT PROGRAM

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Website: www.oneinvestmentprogram.ca

May 10, 2013

Trevor Bingler
Director - Municipal Finance Policy Branch
Ministry of Municipal Affairs and Housing
13th Flr, 777 Bay St
Toronto, ON M5G 2E5

Dear Mr.Bingler:

Re: One Investment Program Request for Amendments to the *Municipal* Act Eligible Investment Regulation

We provide this letter in response to a request for information from Tanya Wanio related to the LAS and MFOA/CHUMS request for changes to the Eligible Investment Regulation. Our request was tabled in writing and verbally with the Debt and Investment Committee at the December 2012 meeting.

In our December 2012 submission, LAS and CHUMS, as agents for The One Investment Program, requested the following changes to the *Municipal Act Eligible Investment Regulation*:

Fixed Income

- *That the Eligible Investment regulation be changed to make 'BBB' rated issues an eligible investment option for The One Investment Program.*

Equities

- *That the list of eligible investments for The One Investment Program be expanded to include Real Estate Investment Trusts (REITS).*

Eligible Program Investors

- *That AMO/LAS, MFOA/CHUMS and other Ontario municipal associations, and their subsidiary companies, be added to the list of 'eligible investors' with whom municipalities can 'comingle' investments.*
- *That consideration be given to allowing First Nations groups the ability to invest in The One Investment Program.*

The One Investment Program track record which supports this 'ask' is articulated in our original submission report – included as Appendix A. In short, the One Program has offered Ontario municipalities and other Ontario public sector entities competitive investment options dating back to 1993 for our Bond Portfolio offering, 1995 for the Money Market Portfolio, 2007 for the Equity Portfolio and since 2008 for the Universe Corporate Bond Portfolio.

JOINTLY ADMINISTERED BY LAS & CHUMS FINANCING CORPORATION - SERVING ONTARIO'S PUBLIC SECTOR.

One Investment Program Performance (returns are net of fees)

Money Market Portfolio	• Average 5 year portfolio balance ending December 31, 2012 = $259 million
	• Annualized Return for 5 years ending December 31, 2012 = 1.52%
	• # of negative month end returns since 1995 portfolio inception = 2
Bond Portfolio	• Average 5 year portfolio balance ending December 31, 2012 = $149M
	• Annualized return for 5 years ending December 31, 2012 = 4.01%
	• # of negative rolling 1 year returns since 1993 inception = 3
Universe Corporate Bond Portfolio	• Portfolio Balance at December 31, 2012 = $39M
	• Annualized 4.5 year return at December 31, 2012 = 5.94%
	• Portfolio inception was August 2008
Equity Portfolio	• Portfolio Balance as at December 31, 2012 = $84M
	• Annualized 6 year return as at December 31, 2012 = 2.91%
	• Portfolio inception was January 2007

The Case for including BBB Rated Issues in One Bond and Corporate Bond Portfolios

In the period since LAS and MFOA/CHUMS tabled our requested changes, Tanya Wanio approached staff for additional supporting information. We request that the Ministry consider the following information before any amendment decisions related to the Eligible Investment Regulation are made.

The following information obtained from both Moody's Investors Service and MFS McLean Budden demonstrates a very favourable experience related to the addition of BBB credits to a bond portfolio. The Annual Default Study: Corporate Default and Recovery Rates, 1920-2012 released by Moody's Investors Service on February 28, 2013 is included with this letter. The pertinent points from this document related to our request are summarized below:

- Of the 58 global corporate issue defaults occurring in 2012, only one was rated as investment grade (exhibit 16, page 19). Investment grade is defined as "BBB3" or higher by Moody's.[1]

- Of total global corporate issue defaults in 2012, only one default was a Canadian corporation (exhibit 16, page 19). This corporation, Catalyst Paper Corporation was not rated investment grade.

- Over the 31-year period from 1982 to 2012, the average annual loss for all BBB rated global credit was 0.13%. In 14 of these years, the annual loss for all BBB rated issues was 0%. There are two instances in the last five years when the loss by A rated credits exceeded the loss incurred by BBB credits (exhibit 23, page 26)

- For the period of 1920 – 2012, there were zero BBB defaults in 60% of the years (exhibit 30, pages 31-33).

[1] The Ratings Table is found on the Multiple Markets website at the following link http://multiple-markets.com/3ratingschart.htm

- The mean difference in default rates between A and BBB graded corporate issues over the period of 1994 to 2012 was only 0.017% in favour of the A graded issues (exhibit 39, page 40).

We would note that with the One Investment Program, professional investment portfolio managers control all investment risk within our allowable investment universe. In the case of the One Bond and Universe Corporate Bond Portfolios, our portfolio manager, MFS McLean Budden, has more than 50 years of experience with a track record of zero defaults.

MFS McLean Budden is of the opinion that there are numerous benefits related to the introduction of BBB-rated bonds into the Eligible Investment Regulation for the One Investment Program. Their submission to the One Program is attached as Appendix B.

In the context of an overall Canadian investment grade bond portfolio, there are several potential benefits to introducing BBB-rated bonds:

- **Enhanced yield**: BBBs generally offer higher yields than higher-grade issues in order to compensate the investor for the additional perceived risk.
- **Capital appreciation**: An investment in BBBs may generate capital appreciation in the event of improving company fundamentals, an upgrade, or healthier macroeconomic landscape.
- **Spread cushion**: BBBs possess a spread cushion that should provide some measure of protection for total return in the event that interest rates rise.
- **Diversification**: BBBs have lower correlations to other sectors of the bond market relative to higher-grade bonds and therefore provide diversification benefits.

Adding an allocation to BBB-rated corporate bonds to a portfolio has the potential to enhance the overall yield and return. Over the past 20 years, the spread between BBB and A rated corporate bonds – the BBB/A quality spread – has averaged 74 basis points (bps) within the DEX Short Term Bond Index and 61bps within the DEX Universe Bond Index over the same period. (Source: PC Bond) MFS McLean Budden (MFS MB) also points out that an annualized 10-year return from a portfolio with a 10% allocation to BBB credit was actually 14 bps higher while having a lower risk profile.

While noting that BBB rated bonds carry greater risk than do higher grade issues they note that appropriate risk management processes should be put in place, to limit position sizes on individual BBB issues or issuers and a maximum allocation limit to BBB credits within a portfolio. At MFS MB, in addition to limits for BBB securities, risk is further controlled through rigorous in-house credit analytics, which augments the work done by the credit rating agencies.

The in-house credit analysis capacity at MFS MB offers municipal investors in the One Universe Corporate Bond Portfolio a significant benefit, with the benefit continuing if the portfolio was to include BBB credits. Most municipalities acknowledge that they do not have the internal staff resources required to properly analyze, review and monitor these credits, whereas, MFS MB has a team of six dedicated credit analysts and extensive systems that support thorough reviews, analyst recommendations, portfolio analysis, trading, and compliance.

The Case for REITS in the One Equity Portfolio

As outlined in our December 2012 submission to the Debt and Investment Committee, the customized portfolio benchmark adopted by LAS and MFOA/CHUMS for the One Equity Portfolio has helped account for the overweight (risky) positions of various sectors (financial, energy, and materials); there however remains a challenge in constructing a suitably diversified, conservative portfolio for our municipal investors. REITs, which are currently not an eligible investment for Ontario municipalities, are contained within the financial sector of the S+P/TSX Composite Index. By allowing these securities for the One Investment Program, the One Equity Portfolio would have the opportunity to increase diversification in the financial sector beyond traditional banking and insurance company holdings. In certain market cycles, the ability to hold securities other than banks or insurance companies may help the One Portfolio reduce overall investor risk, and possibly lead to enhanced returns.

Since its 2007 inception, the One Equity Portfolio has been managed by Guardian Capital LP. Guardian Capital has a specialty practice in managing REIT portfolios and is very familiar with quality-oriented REITs in Canada. As at February 2013 there were 15 REITs included in the S+P/TSX Composite Index. As with all asset classes, the quality of these securities varies, however, Guardian has advised LAS and CHUMS that there is a sufficient universe of quality REIT issues to consider for the One Equity Portfolio.

The attached memo from Guardian (Appendix C) supports our request for the allowance of REITs as an eligible investment for Ontario municipalities and the One Investment Program.

As was the case with the request to add BBB bonds, when considering the addition of REITS we would reiterate that the One Investment Program co-mingled investment portfolios are professionally managed by accredited investment firms. In the six years that the One Equity Portfolio has been in operation with Guardian Capital as the investment manager, the portfolio has outperformed the S&P TSX index on an annualized basis.

Eligible Program Investors

Since tabling our December 2012 proposal, LAS AND CHUMS staff has learned that some committee members believe that allowing AMO/LAS and MFOA/CHUMS to be eligible investors related to the One Investment Program may be a conflict of interest given our role in operating the portfolios. We would respectfully suggest that this is not the case. With respect to the operation of the One Investment Program portfolios, all portfolios are professionally managed to an approved set of investment guidelines that are developed by One staff in close consultation with out independent CFA consultant, our municipal program advisory committee, and the investment managers themselves.

After the investment guidelines are developed for any portfolio they are approved by the LAS and MFOA/CHUMS Boards of Directors. Subsequently all investment decisions are the sole responsibility of the professional investment managers, within the confines of the portfolio guidelines. To be clear, neither LAS nor MFOA/CHUMS staff has any say in the investment decisions related to any One Investment Program portfolio, and due to the success of the portfolios we would like the opportunity to invest along with our municipal investors.

Both AMO/LAS and MFOA/CHUMS believe that through the One Investment Program we provide competitive professionally managed investment options to the municipal sector and that we do so for a very reasonable fee. Through economies of scale, the One Program achieves pricing and options that may not otherwise be available to many small and medium-sized municipalities, and both AMO/LAS and MFOA/CHUMS would like the same opportunity to utilize these investment options.

LAS and MFOA/CHUMS staff also see the value of the One Program extending beyond Ontario municipalities. We would like to see the Eligible Investment Regulation amended to allow First Nations groups to be deemed eligible investors for the purposes of municipal investment co-mingling. Based on the informed advice of our independent CFA, who has a strong background in first nations issues, we believe there is an opportunity to help smaller First Nations groups achieve better investment returns.

We would like the opportunity to meet with you to discuss our December 2012 proposal as well as this letter in greater detail. LAS and MFOA/CHUMS do feel that our proposals are very sound and reasonable requests and feel that you will feel the same way if you have the opportunity to meet with us and our professional investment managers. We look forward to hearing from you to arrange a meeting.

Sincerely,

Daniel Cowin

Dan Cowin
Executive Vice President
CHUMS Financing Corporation

Nancy Plumridge
President
Local Authority Services Limited

/encl

CC: Edward Hankins – Region of York – member of Debt & Investment Committee and One Investment Program Advisory Committee

Gerry Mahoney – City of Ottawa – member of Debt & Investment Committee and One Investment Program Advisory Committee

Appendix A

LAS and CHUMS Submission to the Debt and Investment Committee

Request for changes to the Eligible Investment regulation for the One Investment Program

December 2012

Executive Summary

Since the last substantial change to the Municipal Act Eligible Investment Regulation with O. Reg. 655/05, LAS and CHUMS have worked diligently to educate the Ontario municipal sector about available investment options, opportunities, and related obligations. LAS and CHUMS have also leveraged the expanded investment powers offered to the One Investment Program via O. Reg. 655/05 to develop and launch a successful Canadian Equity Portfolio and a Universe Corporate Bond Portfolio, which complement the existing One Money Market and One Bond portfolios.

With a track record of 6 years of equity investment, 4.5 years of corporate bond investment, and 19 years of money market and bond investment, the One Program is requesting further changes to the Eligible Investment regulation to provide greater investment powers to the One Investment Program.

In addition, LAS and CHUMS is also interested in a broadening of the 'eligible investor' term related to who Ontario municipalities can co-mingle their investments with. AMO/LAS and MFOA/CHUMS, among other municipal associations, would like the ability to invest in the One Investment Program.

Our requested changes are:

Fixed Income

- That the Eligible Investment regulation be changed to make 'BBB` rated issues an eligible investment option for the One Investment Program.

Equities

- That the list of eligible investments for the One Investment Program be expanded to include Real Estate Investment Trusts (REITS).

Eligible Program Investors

- That AMO/LAS, MFOA/CHUMS and other Ontario municipal associations, and their subsidiary companies, be added to the list of 'eligible investors' that municipalities can 'comingle' investments with
- That consideration be given to allowing First Nations groups the ability to invest in the One Investment Program.

1

Introduction

Local Authority Services Limited (LAS) and The CHUMS Financing Corporation (CHUMS), subsidiary companies of the Association of Municipalities of Ontario (AMO) and the Municipal Finance Officers Association of Ontario (MFOA), respectively, have collectively operated the One Investment Program for the Ontario municipal sector since 1993. Until 2010, the program was operated under the name of 'One – The Public Sector Group of Funds' or the One Funds.

It is the intent of this report to demonstrate how the One Investment Program has long offered competitive investment options that are safe and credible for our core investors (i.e. municipalities), with a mind toward minimized investor risk. In addition, based on the One Program's lengthy evidence of thoughtful program design and operation, we are seeking additional investment powers for the program.

One Investment Program Background (including activity since O. Reg. 655/05)

From inception until 2007, the One Program offered two investment options to Ontario municipalities: a short-term Money Market Portfolio and a medium-term Bond Portfolio. In 2005 One was granted additional investment powers under the Municipal Act Eligible Investments regulation (via O. Reg. 655/05), which granted One the ability to invest in longer term corporate debt instruments and shares of Canadian corporations. These expanded investment powers were offered to the Ontario municipal sector only via the One Program. These changes resulted in the launch of a long-term Equity Portfolio offering by One in 2007, and a medium-long term Universe Corporate Bond Portfolio offering in 2008.

When One was given the expanded investment powers through O. Reg. 655/05, a comprehensive assessment process was undertaken to determine how the new investment powers could be turned in appropriate investment options for the Ontario municipal sector. In addition, One also sought to develop a defensible governance and oversight framework for these new expanded investment powers. The first step in One's review was to identify an appropriate independent investment consultant to assist in guiding this process. A CFA with an expertise in foundations, first nations, and not-for-profit clients, was selected to aid LAS and CHUMS, and this individual continues to be retained by One to this date.

One then assembled a 'Working Group' of municipal finance representatives who were interested in assisting in the development of a framework for the new One Program investment portfolios, which also addressed concerns over investment risk and liquidity. The Working Group was composed of representatives from municipalities of various sizes to ensure that all potential One Program stakeholders had a voice in the development of the new investment strategies.

The group established that the first priority in the development of any new longer-term investment mandates for One, or the review of the existing One Program investment mandates (i.e. Money Market and Bond Portfolio) should be risk control and return enhancement. This focus was evidenced in the 2007 revision and expansion of the fixed income investment policies, and also the creation of a conservative equity investment framework.

A summary of the review and activities of the working group related to the One Program investment offerings is as follows:

Fixed Income

Through the municipal working group, One undertook a review of how municipal investors were using the existing Money Market and Bond Portfolios, and whether there were changes that could be made to the portfolios, to ensure a better match between municipal investment horizons and the management of the portfolios.

One staff and the working group also consulted with the current investment managers and the external CFA consultant to identify opportunities and risks related to an expansion of the investment mandate, both from an investor and also a portfolio perspective. Small changes were made to the investment guidelines related to the One Bond Portfolio, but more significant changes for the Money Market Portfolio resulted from this review process:

1) Change of the portfolio management guidelines, including lengthening the average term of the existing portfolio to better reflect actual investment time horizons.
2) Change of the portfolio benchmark from the 30 day T-bill index to the 182 T-bill index.
3) Change of portfolio manager to achieve a more focused and advantageous investment strategy, consistent with investor expectations.

The review also found a need for a medium-long term bond investment option for the sector, given the new powers granted to the One Program via O. Reg. 655/05. It was deemed appropriate to launch a new corporate bond portfolio, rather than altering the focus and purpose of the existing short-medium term One Bond Portfolio, as it may have resulted in some inappropriate investments by existing portfolio investors.

A new Universe Corporate Bond (UCB) Portfolio was designed to provide municipal investors the ability to better match the time horizon of the securities with the time horizon of longer term liabilities. The portfolio is managed to have a similar duration as the DEX Universe Bond Index, in keeping with the long term nature of infrastructure reserve funds. In addition it provides investors with the opportunity to improve earnings through its focus on very high quality corporate issues.

Shares of Canadian Corporations

O. Reg. 655/05 also provided municipalities with the ability to invest in Canadian equity investments, but this power was granted only through the One Investment Program. Although a desirable expansion of the investment regulation, this new investment opportunity presented a significant challenge for the One Program, in that only 'shares of Canadian corporations' are eligible investments and the Canadian equity market is limited in terms of quality and diversification by both industry sector, and specific securities.

In 2006, One staff, along with our independent CFA consultant and working group, set to develop investment guidelines for the portfolio. It was discovered that the Canadian equity market was heavily dominated by three sectors: Financials, Materials and Energy, which represented a total of 75.9% of the market capitalization of the S&P / TSX Composite Index at December 31, 2006 – see below table. In addition, of the remaining sectors there was a limited selection of high quality companies that had proven track records of stable performance and steady dividends, which is exactly the type of investment desired by the One Program for our municipal investors.

SECTOR	At December 31, 2006	
	S&P /TSX Composite	MSCI World
Consumer Staples	2.6%	8.0%
Consumer Discretionary	5.2%	11.4%
Industrials	5.3%	10.7%
Utilities	1.5%	4.4%
Telecom Services	5.0%	4.5%
Energy	27.9%	9.1%
Information Technology	3.7%	10.4%
Healthcare	0.8%	9.2%
Financials	31.9%	26.4%
Materials	16.1%	6.0%

In contrast, the global equity markets were, and continue to be, more broadly diversified across the industry sectors, as demonstrated in the table below.

Group & Sector Allocations at Jan 2007		
MSCI World GIC Sector	**MSCI World Sector Weightings**	**S&P TSX Sector Weightings**
Resource	**15.10%**	**44.00%**
Energy	9.10%	27.90%
Materials	6.00%	16.10%
Consumer	**28.60%**	**8.60%**
Health Care	9.20%	0.80%
Consumer Discretionary	11.40%	5.20%
Consumer Staples	8.00%	2.60%
Interest Sensitive	**30.80%**	**33.40%**
Financials	26.40%	31.90%
Utilities	4.40%	1.50%
Industrials	**25.60%**	**14.00%**
Industrials	10.70%	5.27
Information Technology	10.40%	3.72
Telecom Services	4.50%	4.97

The challenge faced by the One Program given the above facts, was to design a portfolio structure that would minimize risk, ensure appropriate diversification, and remain compliant with the Municipal Act Eligible Investment regulation limitation to invest only in shares of Canadian corporations. This challenge is not faced by other similar institutional investors, including Housing Services Corporation (formerly Social Housing Services Corporation), OMERS, and Teachers; these organizations have the ability to gain effective diversification while maintaining liquidity through the inclusion of Income Trusts, Real Estate Investment Trusts as well as shares of non-Canadian issuers.

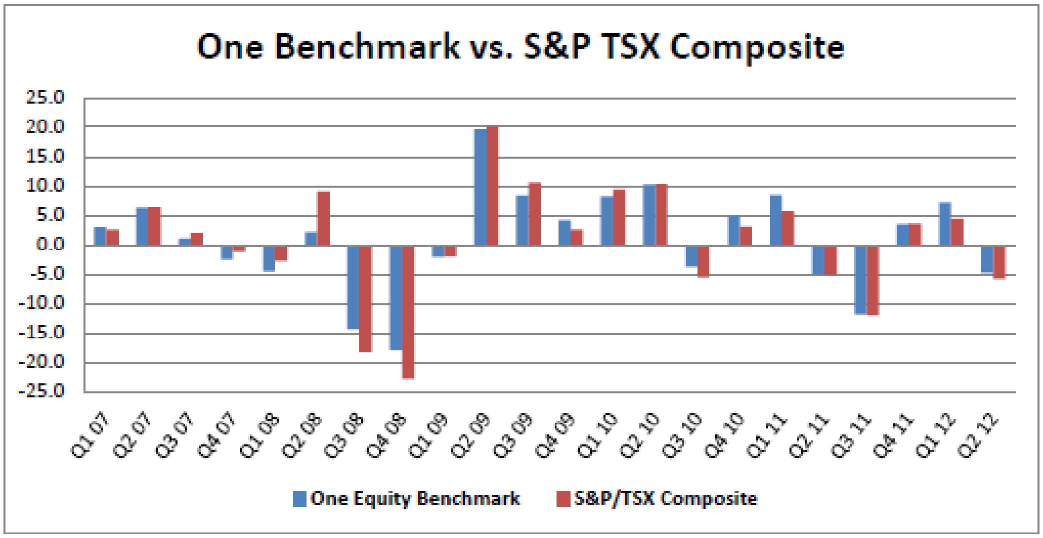
In addition, as a broad, diversified investment universe was not available to One, a customized portfolio structure was designed for the One Equity portfolio to ensure a minimal amount of risk and maximum investment diversification for municipal investors.

The portfolio structure developed by One requires the portfolio manager to maintain broad industry diversification similar to that exhibited in global equity markets (via the MSCI world sector weightings) while still adhering to the Municipal Act Eligible Investment regulation limitation of investment in only shares of Canadian corporations. The One portfolio benchmark superimposes the MSCI world sector weightings over the S&P/TSX to create a diversified portfolio of eligible investment options for the One Equity Portfolio. The benchmark is reviewed and amended twice each year; the original allocation for the One Equity Portfolio is below.

Group & Sector Allocations as at Jan 2007

Group	MSCI World GIC Sector	MSCI World Sector Weightings	S&P TSX Sector Weightings	Relative Minimum	Relative Maximum	Actual Minimum	Actual Maximum
Resource		**15.10%**	**44.00%**	50%	150%	7.55%	22.65%
	Energy	9.10%	27.90%		2 times sector weight		
	Materials	6.00%	16.10%				
Consumer		**28.60%**	**8.60%**	75%	125%	21.45%	35.75%
	Health Care	9.20%	0.80%		2 times sector weight		
	Consumer Discretionary	11.40%	5.20%				
	Consumer Staples	8.00%	2.60%				
Interest Sensitive		**30.80%**	**33.40%**	75%	125%	23.10%	38.50%
	Financials	26.40%	31.90%		2 times sector weight		
	Utilities	4.40%	1.50%				
Industrials		**25.60%**	**14.00%**	75%	125%	19.20%	32.00%
	Industrials	10.70%	5.27		2 times sector weight		
	Information Technology	10.40%	3.72				
	Telecom Services	4.50%	4.97				

Over the six years the One Equity Portfolio has been available to municipal investors, the portfolio has performed as expected by balancing risk management with reasonable performance over the longer term. This is evidenced in the below chart with a comparison to the S&P TSX performance.



During the North American credit crisis of 2008, the design of the One Equity Portfolio provided significant capital protection to investors, consistent with its design. With the custom benchmark, the One Equity Portfolio was designed to minimize, as much as possible, extreme negative returns through appropriate diversification, while also providing near market returns on the upside. In short, the One Portfolio was designed not to chase returns in a rising market; instead the portfolio invests in proven and predictable companies that continue to grow over time.

To ensure effective oversight, risk control, and portfolio operation, LAS and CHUMS staff continue to review the portfolio operation periodically, and the One Program Advisory Committee formally meets with the portfolio manager semi-annually.

A formal review of all four current One Program portfolios is conducted annually by One's independent CFA consultant, in order to assess if the performance of the One Program portfolios are acceptable, both from a returns perspective but also a risk management perspective. The findings of these annual reviews are shared by LAS and CHUMS with the One Program Advisory Committee, and are also summarized in the program's year-end report to investors.

One Program Commitment to Investor Education and Support

LAS and CHUMS believe that developing an appropriate investment portfolio approach is not enough; since the expanded investment powers were granted to the One Program via O. Reg. 655/05, LAS and CHUMS have undertaken a committed effort to educate municipal staff and elected officials about the investment options available to them, their related responsibilities, investment strategies, and opportunities related to the One Investment Program. Our belief is that no investment option should be considered by a municipality if the investor is not aware of the investment type, potential risks, etc.

Since receiving enhanced investment powers for the One Program in 2005, LAS and CHUMS have provided education and support through multiple channels, including conference presentations at various MFOA and AMO conferences and events, targeted presentations to municipal administrator/treasurer groups, telephone availability, robust website information, as well as quarterly investment program reports that are pushed out to key individuals within the Ontario municipal sector. LAS and CHUMS have also delivered 'Investment 101' educational seminars to more than 235 municipal staff and elected officials on investment powers, opportunities and responsibilities since 2009.

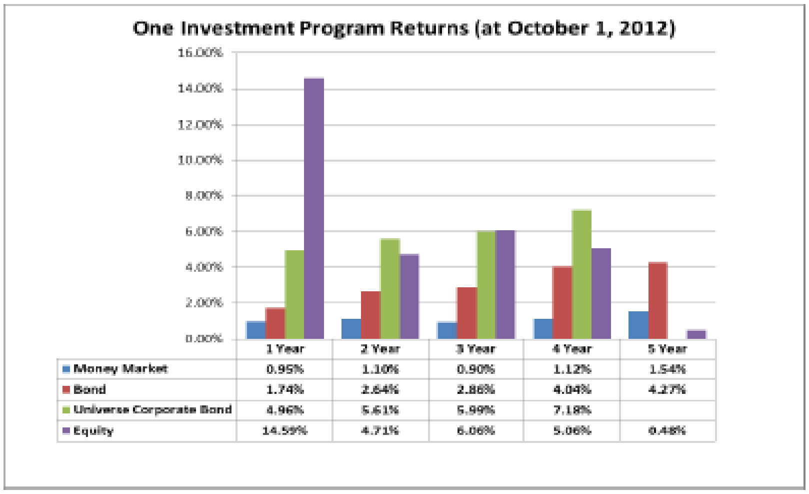
In addition to sector outreach, staff has made great efforts to ensure that investors and potential investors are aware of the appropriate investment duration for all monies invested in any of the One Program portfolios. An example of our education is the below table from our marketing collateral:

Portfolio	Intended Investment Duration	Investment Approach	Holdings
Money Market	1 month to 18+ months	Preserve capital and maintain liquidity while maximizing short-term income	• Canadian treasury bills • High quality commercial paper • Banker's acceptances • Floating rate notes
Bond	18 months to 3+ years	Provide a higher return over longer investment horizons through diversified investments	• Federal, provincial and municipal bonds • High quality bank paper • Bank guaranteed debt
Universe Corporate Bond*	4+ years	Investment in highly rated corporate bonds maturing over a wide timeframe	• Canadian corporate bonds • Federal, provincial and municipal bonds
Canadian Equity*	5+ years	A diversified, conservatively managed portfolio of equity securities issued by Canadian corporations	• Canadian equity securities

* Available to Ontario municipalities only through One Program as per the Municipal Act Eligible Investment regulation

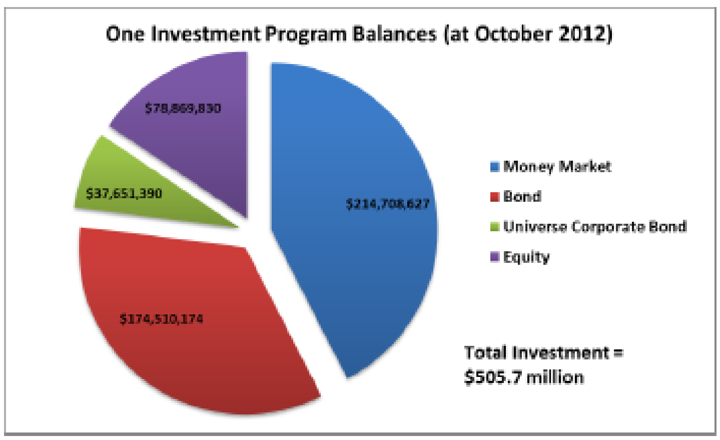
One Investment Program Results

The results of the One Programs commitment to provide municipalities with a greater understanding of both the benefits and the risks of investment through education, and also the opportunity to better match their investments to their short and long term liabilities has been proven. Despite the challenges noted in this report, 'early adopter' municipalities in both the One Universe Corporate Bond Portfolio and Equity Portfolio have benefitted from enhanced investment returns – see the three and four year returns for both the One Universe Corporate Bond Portfolio and Equity Portfolio below, which are presented on a net of fees basis.



	1 Year	2 Year	3 Year	4 Year	5 Year
Money Market	0.95%	1.10%	0.90%	1.12%	1.54%
Bond	1.74%	2.64%	2.86%	4.04%	4.27%
Universe Corporate Bond	4.96%	5.61%	5.99%	7.18%	
Equity	14.59%	4.71%	6.06%	5.06%	0.48%

The consistently demonstrated focus on strong governance, program oversight, and risk controls has been recognized by One investors and is a key reason for their continued participation in the program. At October 2012, total investment in the four One Program portfolios totaled almost $506 million – as below.



Proposed Revisions to Eligible Investment Regulations

One has demonstrated an ongoing commitment to risk control and strong oversight while evolving the mandates of each of the portfolios to provide competitive and diversified investment options to our municipal investors. To continue with this mandate, LAS and CHUMS propose the following amendments to the Eligible Investment regulation as it relates to the One Investment Program.

Fixed Income Investment

Our ask: We request a change to the Eligible Investment regulation to make 'BBB` rated issues an eligible investment option for the One Investment Program and our municipal investors.

A challenge for the One Universe Corporate Bond Portfolio is the credit quality restrictions within the current Eligible Investment regulation. These restrictions severely limit the investable universe for this portfolio as the following tables demonstrates.

DEX All Corporate Bond Index		
	% of Index	
	Issues	Market Value
AA	15.8%	29.0%
A	49.0%	43.3%
BBB	35.1%	27.7%

The current credit quality restrictions on Corporate issues with greater than five years to maturity excludes 35.1% of the available investment grade issues and 27.7% of the investable universe defined by the market value of issues within the index.

In addition, with short-term interest rates at or close to record lows, our municipal investors find themselves in a yield-starved environment.

Adding an allocation to BBB-rated corporate bonds has the potential to:

- Enhance the One portfolio's overall yield and total return
    - over the past 20 years, the spread between BBB and A rated corporate bonds – the BBB/A quality spread – has averaged 0.74% within the DEX Short Term Bond Index and 0.61% within the DEX Universe Bond Index over the same period. (Source: PC Bond)

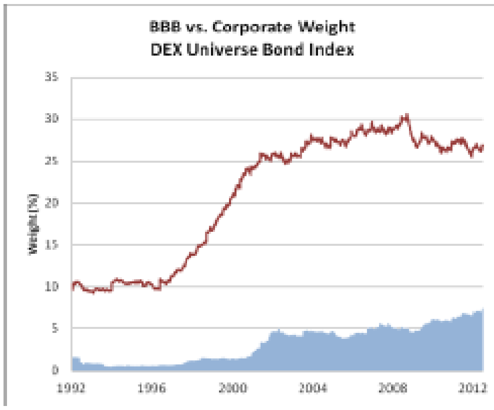
- Offer diversification benefits due to their lower correlations to other sectors of the bond market and can enhance risk-adjusted returns
    - Using ten years of historical data from the DEX Short Term Bond Index, adding BBB corporates in their Index weight of approximately 5% boosts the average annual total return by 0.05% while reducing the standard deviation of returns. (Source: PC Bond)

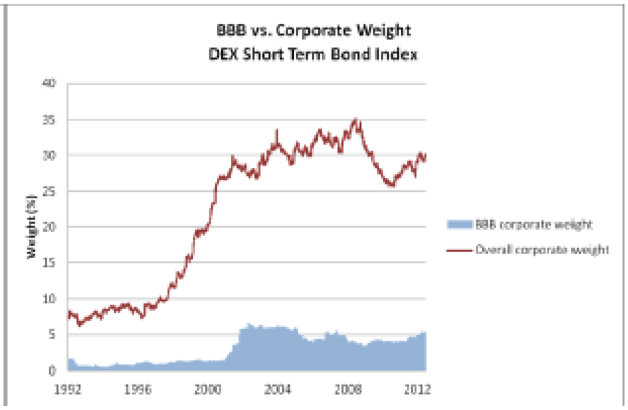
- Provide a measure of total return in the event that interest rates rise, given the spread cushion.

Size Matters

The corporate bond market has grown considerably and now represents a significant share of the overall bond market in Canada. As the charts below illustrate, corporate bonds have grown from below 10% of the universe of bonds to almost 30%. Growth in the weight of BBB-rated corporates has been just as robust, 7.5% of the DEX Universe Bond Index and 27% of the Index's overall corporate weight (Source: PC Bond, as of June 30, 2012).

As of the end of the second quarter 2012, the size of the BBB-rated corporate bond market in the DEX Universe Bond Index was $87 billion and includes such Canadian household names as Rogers, Loblaw, CP Rail, and Enbridge (Source: PC Bond).



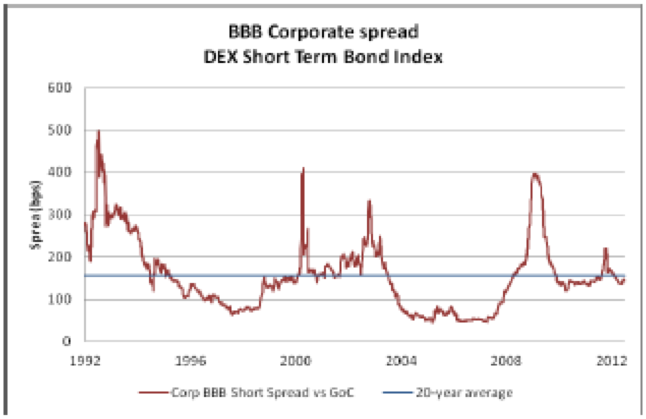


Given the increase of BBB-rated corporate bonds, there is a much larger benchmark risk than there was 20 years ago associated with a portfolio that prevents investment in lower-rated investment grade (i.e. BBB) issues.

Why consider allowing BBBs for the One Program portfolio?

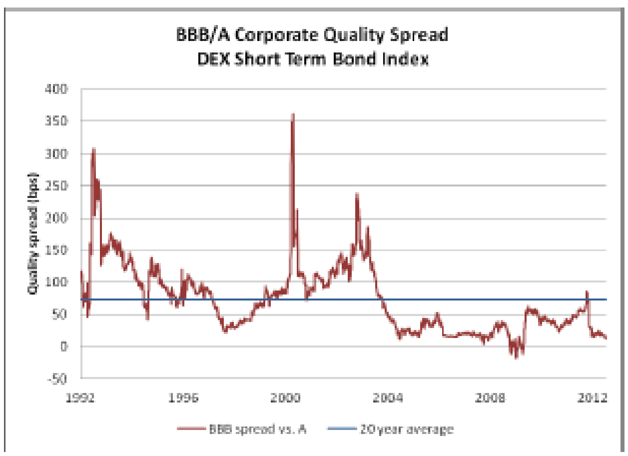
- **Capital appreciation**: An investment in BBBs may generate capital appreciation in the event of improving company fundamentals, an upgrade, or a healthier macroeconomic landscape.
- **Spread cushion**: BBBs possess a spread cushion that should provide some beneficial measure for total return when interest rates rise.
- **Diversification**: BBBs typically have had lower correlations to other sectors of the bond market relative to higher grade bonds and therefore may provide diversification benefits.
- **Enhanced yield**: BBBs generally have offered higher yields than higher-grade corporates in order to compensate investors for the slight additional risk.

Naturally, in the current yield-starved environment, the last bullet point is the most attention grabbing. A scarcity of income due to unprecedented low interest rates has made the yields offered by lower-grade issues especially attractive. The following chart shows the spread relationship between BBB-rated corporates and Government of Canada issues within the DEX Short Term Bond Index. (Source: PC Bond, as of June 30)



Clearly, this spread fluctuates over time, generally widening during times of market stress and narrowing during periods of more stable and healthy economic growth. As of the end of the Q2 2012 this spread was approximately equal to its twenty year average of 1.55%.

Furthermore, BBB corporates have offered a positive spread vs. those assigned an A rating, averaging 0.75% over the past twenty years. The BBB/A spread has narrowed since 2004, but has still averaged 0.33%. (Source: PC Bond, as of June 30)



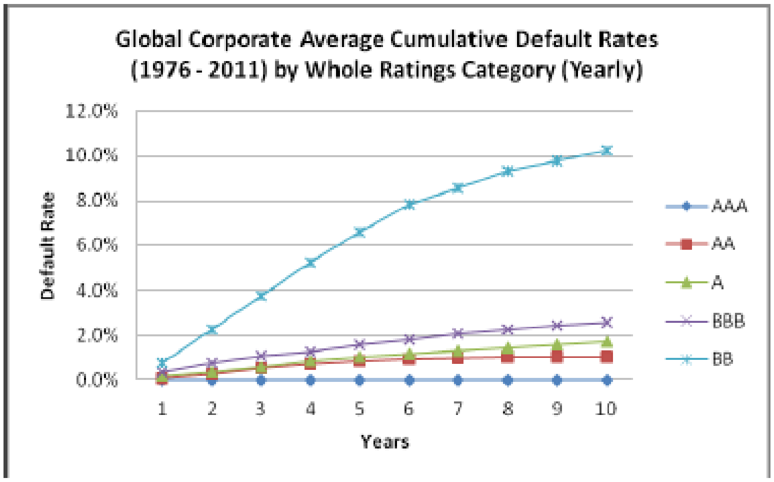
What are the risks?

The prospect of higher yield and total return comes with a trade-off: slightly increased risk. Broadly-speaking, this higher risk stems from the higher credit risk associated with BBB issuers. Spreads can widen due to company-specific or macro-level concerns, a bond's price can fall as a result of a downgrade, or the issuer can default by failing to meet its interest or principal payments.

11

Default Risk

Default risk is the risk that a bond issuer will be unable to make the required payments on their debt obligations. Historically, the Canadian bond market does not have a notable history of defaults. In a study published earlier this year, ratings agency DBRS looked at all the corporate issuers for which it had assigned ratings from 1976 through 2011. The following chart shows the average cumulative default rates by rating over that period:



Source: DBRS (http://dbrs.com/research/246789/2011-dbrs-corporate-rating-transition-and-default-study.pdf)

For instance, 5 years after having assigned an issuer a rating, those with a rating of A had a 1.0% cumulative probability of default, whereas those with a rating of BBB had a 1.6% probability of default. As expected, the risk of default is greater for BBBs, however the differential between BBBs and other investment grade issues is much smaller than the differential between investment and non-investment grade (i.e. below BB).

Furthermore, it can be argued that the extra yield generated by BBB issues more than compensates for the incremental additional risk of default. In other words, even if there are more defaults in the BBB space, the additional total return provided by those BBB issues that remain solvent may be adequate to offset the additional risk.

In summary, broadening of the issues eligible for investment by One to allow for 'BBB` issues would allow the portfolio the ability to offer better diversification of both issuers and sector exposures. The increase in eligible issuers would enable One to access the entire universe of corporate issues and provide better diversification within the portfolio.

Equity Investment

Our ask: We request that the list of eligible investments for the One Investment Program be expanded to include Real Estate Investment Trusts (REITS).

Even with the customized portfolio benchmark for the One Equity Portfolio, we continue to face challenges in constructing a suitably diversified, conservative portfolio for our municipal investors. This is particularly evident in the limited Canadian market universe in the Consumer Staples, Healthcare, Utilities, Real Estate and Telecom Services sectors, for large capitalization, stable, dividend paying companies. In particular within the Real Estate sector the security profile that is most suitable to the One portfolio is typically found in Real Estate Investment Trusts rather in within corporate issues.

__Eligible Program Investors__

1) **Our ask: We request that AMO/LAS, MFOA/CHUMS and other Ontario municipal associations, and their subsidiary companies, be added to the list of 'eligible investors' that municipalities can 'comingle' investments with. This would allow municipal associations the ability to invest in the One Investment Program.**

Currently AMO/LAS and MFOA/CHUMS are not eligible investors for the One Investment Program due to the co-mingling restrictions within the Eligible Investment regulation. Allowing these organizations, and all other Ontario municipal associations, to invest alongside the current municipal investors would further align the interests of investors with the interest of the program sponsors. This would ensure that a key governance principle of aligning stakeholders' interests with management / operators could be demonstrated in the One Investment Program. The ability to invest in the One Program is a request that has also been made by a variety of AMO and MFOA sister municipal associations (i.e. AMCTO, NOMA, etc.) in recent years.

2) **Our ask: We request consideration related to providing First Nations groups the ability to invest in the One Investment Program.**

Another group that could potentially benefit from eligibility to invest through the One Program is First Nations. While it is true that many First Nations are poor there are also many who are not and who manage substantial budgets. Our independent CFA consultant has tremendous experience with First Nations groups and has noted that many would have an interest in a pooled investment option like the One Investment Program. First Nations in British Columbia are currently entitled to invest in the MFABC pooled funds and many do participate. Many Fist Nations receive funds from industry as a result of Impact Benefit Agreements, and others retain settlements resulting from land claims that are investable monies for the First Nation government.

Granting First Nations organizations eligibility to invest through One would provide an additional option for these historically disadvantaged communities to obtain competitive rates of return within a strong governance framework. We request that this option be considered by the Province.

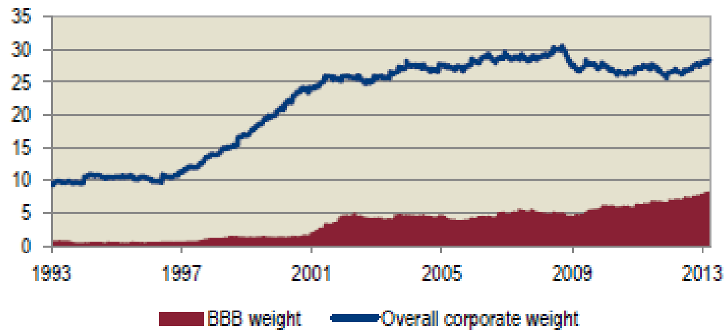
Appendix B

BBB-rated bonds: An essential component of a well-diversified, investment grade Canadian bond portfolio

Market size:
BBBs represent a growing proportion of the Canadian bond market

Corporate bonds are an increasingly important part of the Canadian bond market. As illustrated in the chart below, corporate bonds now represent almost 30% of the investible universe. More and more companies – both Canadian and non-Canadian – are issuing bonds in Canada.

DEX Universe Bond Index Composition



Source: PC Bond, as of March 25, 2013

While the overall corporate weight in the DEX Universe Bond Index has increased over the past 20 years, even more striking has been the growth in BBB-rated names. As of March 25, 2013, the size of the BBB market in Canada was $101 billion, or 8.2% of the DEX Universe Bond Index and 29% of the DEX Corporate Bond Index.

Importantly, we expect this trend to continue.

Risk:
The importance of carefully monitoring the risk of all securities in a portfolio

All corporate bonds, no matter the rating, have an element of default and price risk. As individual securities, BBB-rated bonds carry greater risk than higher-grade issues *in the opinion of the credit rating agencies*. Broadly-speaking, this higher perceived risk stems from the higher credit risk associated with BBB issuers. Spreads can widen due to company-specific or macro-level concerns, a bond's price can fall as a result of a downgrade, or the issuer can default by failing to meet its interest or principal payments. BBB-rated bonds, as individual securities, tend to have higher price volatility. Event risk such as M&A must also be considered, although it is the higher-rated credits and less often BBBs that are typically targeted for M&A activity as the higher-rated credits have a greater ability to add leverage to their balance sheets in order to finance the activity.

As a result, an investment grade portfolio that includes BBB-rated bonds should have appropriate risk management processes in place. These may include limits on position sizes on individual issues or issuers, a maximum allowable allocation to BBB-rated bonds, and most importantly, a fundamental credit research process that identifies and monitors investments from a credit risk perspective. A good bond manager will not rely on the credit rating agencies for credit opinions; rather, a good bond manager, using all the resources at its disposal, will formulate its own opinions on a particular issuer's creditworthiness.

Benefits:
Potential for greater risk-adjusted portfolio returns, and benefits from diversification

In the context of an overall Canadian investment grade bond portfolio, there are several potential benefits to introducing BBB-rated bonds:

- Enhanced yield: BBBs generally offer higher yields than higher-grade issues in order to compensate the investor for additional perceived risk.
- Capital appreciation: An investment in BBBs may generate capital appreciation in the event of improving company fundamentals, an upgrade, or a healthier macroeconomic landscape.
- Spread cushion: BBBs possess a spread cushion that should provide some measure of protection for total return in the event that interest rates rise.
- Diversification: BBBs have lower correlations to other sectors of the bond market relative to higher-grade bonds and therefore provide diversification benefits.

This last bullet deserves further discussion. The benefits of diversification are derived both in terms of names and in terms of industries. For instance, the Canadian telcos are all BBBs: Bell, Telus, Rogers, Shaw. Most industrial names (Cameco, CP Rail) as well as many of the consumer names (Loblaw, Canadian Tire) are BBBs.

The following table – which depicts the corporate segment of the DEX Universe Bond Index – offers some perspective on the diversification benefits of including BBBs in a fixed income portfolio in terms of sectors, names, and issues:

Rating		Communi-cation	Energy	Financial	Industrial	Infra-structure	Real Estate	Securitization	Total
AAA	Size			3 B				9 B	12 B
	# Issues			3				16	19
	# Issuers			1				9	10
AA	Size			76 B		3 B	2 B		81 B
	# Issues			66		9	6		81
	# Issuers			10		3	1		14
A	Size	3 B	27 B	80 B	5 B	40 B	2 B		157 B
	# Issues	4	119	130	15	113	5		386
	# Issuers	2	23	43	7	34	4		113
BBB	Size	33 B	20 B	17 B	18 B	9 B	5 B		101 B
	# Issues	56	72	37	61	29	25		280
	# Issuers	10	22	19	24	9	7		91
	BBB examples	Bell, Rogers, Telus, Shaw	TransAlta, Encana, Union Gas	BMO & CIBC Tier 1 Captial, Ford Credit	Cameco, CP Rail, Cdn Tire, Loblaw	407 Int'l, Nova Scotia Power, Fortis	RioCan REIT, First Capital Realty		
Total	Size	36 B	46 B	176 B	23 B	52 B	8 B	9 B	350 B

Source: PC Bond, MFS McLean Budden, as of March 25, 2013

Simply put, a portfolio consisting solely of AAA, AA, and A-rated bonds would be very heavily weighted in government bonds and financials, which is demonstratively riskier than a well-diversified portfolio that includes BBBs. Using 10 years of DEX Universe Bond Index returns, the following table shows how hypothetical portfolios with varying amounts of BBB-rated bond weights would have performed:

BBB weight[1]	Annualized 10-year return	Annualized standard deviation
0.00%	6.00%	1.98%
5.00%	6.07%	1.92%
10.00%	6.14%	1.91%
15.00%	6.21%	1.94%
20.00%	6.29%	2.01%

Source: PC Bond, MFS McLean Budden

While one may be inclined to believe that risk in the portfolio increases by adding BBBs, a responsible portfolio manager would actually be attempting to better manage risk while seeking better risk-adjusted returns. A 10% allocation to BBBs over the past ten years would have generated a higher return with a lower amount of risk than one with no BBBs. And an 18% allocation to BBBs over the past ten years would have out-yielded a portfolio with a 0% allocation by 26bps with the same amount of risk.

[1] Scenario analysis uses DEX Universe Bond Index weights and returns by sector: Federal bonds, provincial bonds, municipal bonds, AAA/AA corporates, A corporates, and BBB corporates. Non-BBB sector scenario weights derived in proportion to their weight in the Index. Benchmark returns used for the ten-year period ended December 31, 2012.

Appendix C

To: The One Investment Program

From: Brian Holland, Senior Vice President, Guardian Capital LP

Date: March 27th 2013

Re: Rational for the inclusion of Real Estate Investment Trusts in a Canadian Equity Portfolio

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This memo is support of the One Portfolio proposal for allowing Real Estate Investment Trusts as a permissible investment in the One Investment Program Canadian Equity portfolio used by Ontario Municipalities.

Measurement: At the end of February, the S&P/TSX Composite Index has a 2.7% exposure to REITs. One of the central principals of investment management practice is that portfolio results should ideally be measured against a benchmark where the manager can invest in the underlying securities. At present, the One Portfolio Canadian Equity strategy is measured, albeit by a small amount, against the performance of REITs in the S&P/TSX Composite Index and these are not permissible investments.

Performance: Below is a comparison of the S&P/TSX Composite Index versus the S&P/TSX Capped REIT Index[1]. As indicated, this 'sub-group' of assets has performed well.

Comparison of the S&P/TSX Capped REIT Index vs. the S&P/TSX Composite Index (Total Return %) Ending December 31st 2012

	1 Yr	2 Yrs	3 Yrs	4 Yrs	5 Yrs	6 Yrs	7 Yrs	8 Yrs	9 Yrs	10 Yrs
S&P/TSX Cdn REIT Total Return	16.97	19.30	20.39	28.29	10.83	7.89	10.15	11.94	12.16	13.47
S&P/TSX Composite Total Return	7.19	-1.08	4.79	11.65	0.81	2.26	4.28	6.58	7.43	9.22

Portfolio Exposure: Guardian Capital has a specialty practice in managing REIT portfolios and we are therefore very familiar with most of the quality oriented REITs in Canada. Current REITs held in all Guardian Capital portfolios is approximately $600 million. At this time, for the One Portfolio we would be investing in only RioCan, the largest REIT in Canada, specializing in shopping malls and retail facilities. The current yield on this security is 5.17% and its total market capitalization is $8.1 billion. Typically, the portfolio will hold approximately 2% in any one particular investment.

Diversification: REITs are contained within the Financial sector of the S&P/TSX Composite Index. By allowing these securities, the portfolio has the opportunity in to increase diversification in the Financial sector beyond the traditional banking and insurance company holdings. In certain market cycles, the ability to hold securities other than banking or insurance companies may help reduce portfolio risk and/or enhance results.

[1] Note that the S&P/TSX Capped REIT Index is not a sub-set of the S&P/TSX Composite and is shown from illustrative purposes. The REIT membership and weights, therefore, may differ between Indices.

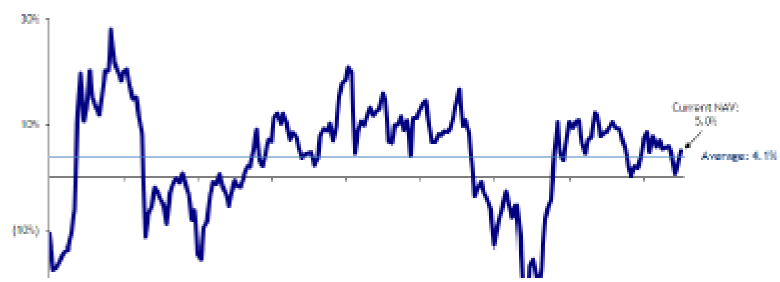
Investment Opportunity: At the end of February 2013, there were 15 REITs included in the S&P/TSX Composite Index. As with all asset classes, the quality of the securities vary, however, as portfolio managers we believe that this is a sufficient number of securities to select from in order to perform our analysis and to make comparisons for valuation purposes.

Characteristics: REITs are generally lower growth securities that pay most of their profits to unit holders. Below is a comparison of market statistics of a selection of REITs versus both the S&P/TSX Composite Index and the Financial sector. This analysis is based on the Morningstar (CPMS) analysis as of March 26th 2013.

	S&P TSX Composite	Financial Sector	Selection of REITs
Number of Securities in Analysis	240	89	22
Expected Yield %	3.09	2.82	4.99
5 yr normalized Dividend growth (%/yr)	8.18	3.76	1.43
Long Term Debt to Equity Ratio	0.47	0.40	0.83
5 yr normalized sales growth (%/yr)	3.99	2.10	-1.66
5 yr normalized earnings growth (%/yr)	6.08	10.49	32.05
10 yr normalized earnings growth (%/yr)	9.42	4.21	5.87
Current Price/Book ratio	1.86	1.13	1.21

Current Valuations: REITs currently looks expensive on some relative index measures but more reasonable when compared to the price-to-net-asset values (NAV) and comparative U.S. REITs. Below is a long term illustration of the valuations of REITs versus their NAV.

<u>Canadian REITs:</u> Public valuation versus value of net asset value of real estate holdings



Source: RBC Capital Markets as of January 31, 2013

Outlook: We expect good cash flow growth into 2013 driven by healthy fundamentals, interest cost savings on debt refinancing, and accretive acquisitions. The sector should continue to benefit from continued stable outlook for commercial property fundamentals, valuation support from direct property markets, low interest rates, attractive relative yields, and good cash flow growth. From a stock selection perspective, we believe it remains prudent to maintain our bias to higher quality, mid to large cap companies at this time.

Appendix D: Position on O. Reg. 284/09 – Budget Expenses

Response to Posted Regulation Changes Under the *Municipal Act*

Section 294.1 of the Municipal Act requires municipalities to prepare financial statements each year in accordance with "generally accepted accounting principles" established by the Public Sector Accounting Board of the Canadian Institute of Chartered Accountants. In early 2010, municipalities will prepare financial statements for 2009 that will require tangible capital asset accounting for the first time. This represents a significant change in municipal accounting practices.

The new rules with regard to TCA accounting will alter the meaning of traditional concepts such as "surplus" and "accumulated surplus." Since the former of these terms is used elsewhere in the Act to set out rules related to budgeting, MFOA has recommended for some time that a review be undertaken of the Act to see if amendments were warranted in light of the pending move to full accrual accounting. The "balanced budget" provisions found in section 289 (upper tiers) and 290 (local municipalities) were obvious candidates for such a review and have received considerable attention in recent years.

The review by the Ministry of Municipal Affairs and Housing has resulted in proposed changes to legislation and regulations to accommodate full accrual accounting. The legislative changes are found in proposed amendments to the *Municipal Act, 2001* in schedule 19 of Bill 162 and amendments to the *City of Toronto Act, 2006* found in schedule 4 of the Bill. In addition, a number of regulations are proposed as well. The Ministry of Municipal Affairs and Housing has posted draft regulations under the *Municipal Act* on the small business registry and is seeking comments from the municipal sector. This is MFOA's response to those regulations.[2]

<u>Balanced Budget Provisions</u>

For several years, Ministry staff has indicated that amendments to the legislation would likely re-establish the status quo ante. The amended Act would mirror the current provisions in sections 289 and 290 with regard to budgeting. The current provisions of section 289 (upper tier budgets) are shown in the Table 1 below.[3] The Table compares section 289 as it exists currently with the way it would exist if the proposed amendments in schedule 19 are passed. Although the wording with regard to the balance provisions found in subsection 289(2) is very different, the policy intent is similar. The key difference is that the legislation, absent any regulations, would require municipalities to finance annually amortization (a non-cash expense) as well as post employment benefits and post closure costs for landfills. The legislation provides the Minister with the authority to pass regulations to specify expenses which can be excluded from a municipal budget. The draft regulation on the small business registry identifies the three expenses above (e.g. amortization, post-employment benefits and post-closure costs for landfills) and states that a municipality can fund part or all of these in a given year. Therefore, the new amendments, read in conjunction with subsection 1 of the proposed regulation dealing with "budget matters-

[2] MFOA is limiting its response to changes to the *Municipal Act* only.

[3] These provisions are mirrored in section 291 that deals with the budgets of local municipalities. The summary shown in Table 1 applies equally to those sections as well.

expenses," delivers on the commitment to reproduce the existing provisions of section 289 with language that is more consistent with full accrual accounting.

Table 1

Current Provisions of *MA 2001* Section 289	Description of Current Section 289	Description of Amended Version of Section 289
289(1)	Requires the adoption of a budget each year (or preceding year)including all sums required during the year, including: • All costs as they come due • Amounts raised for sinking funds, retirement funds, debenture payments • Amounts required to be paid to local boards, excluding school boards Budgets cannot be passed in the "preceding year" if that year is an election year.	Completely unchanged.
289(2)	Budget shall set out estimated revenues and expenditures, including amounts to be raised in general and area specific levies. Estimated revenues must equal estimated expenditures. The Minister may establish rules with regard to the "detail and form" of an upper tier budget	Provisions currently in ss 289(2) are found in ss. 289(2) and 289(3) in very different language but with the same policy intent.
289(3)	Sets out a number of conditions to be met in a budget. It shall provide for: • Any operating surplus or deficit from the previous year. • Taxes and other revenues that are not collectible (in the opinion of the treasurer) In addition, a budget may provide for such reserves and council considers necessary.	Provisions of ss. 289(3) are found largely unchanged in ss. 289(4) of amended version
289(4)	Section 34 of the *Assessment Act* and 353 of the *Municipal Act* apply to upper tier municipalities, with necessary modifications.	Provisions of ss. 289(4) are found largely unchanged in ss. 289(6) of amended version.
289(5)	Where an upper tier must provide money to a board, it may set dates and establish the form for budget submissions from those boards.	Provisions of ss. 289(5) are found largely unchanged in ss. 289((7) of amended version.
289(6)	Part III of the Legislation Act does not apply to the power of the Minister to establish the "detail and form" of an upper tier budget under 289(2).	Provisions of ss. 289(6) are found largely unchanged in ss. 289((8) of amended version.
Note: There is a new ss. 289(5) in the amended version that serves as a transition provision for 2009. It ensures that the 2009 budget will take into account an operating surplus from the prior year and shall make provision for any operating deficit. This replicates the requirements currently in 289(3).		

However, subsections 2, 3 and 4 of the draft regulation add new reporting requirements that have not been previously found in *MA 2001* or regulations. The new provisions require a municipality that is not fully funding the three expenses above to prepare a report to council, beginning in 2010 that sets out:

- An estimate of the change in the accumulated surplus of the municipality or local board to the end of the year.
- An analysis of the estimated impact of the municipality's or local board's recommendations in respect of the expenses listed in section 1 on the future tangible capital asset funding requirements of the municipality or local board.

This report must be adopted by Council by resolution before a budget can be passed. The regulation requires that these reporting provisions be reviewed before the end of 2012. It seems obvious that the intent of these reporting provisions is to require council to confront issues related to the financing of assets (amortization), post employment benefits and post closure costs for landfills as part of the budget process. MFOA fully supports asset management and long-term financial plans that finance assets, operations and growth on a sustainable basis. However, we cannot see the merit in the reporting requirements contained in the regulation in promoting the goal of long-term financial planning.

Not consistent with MA 2001 view of municipalities. In our view, the reporting requirements seem at odds with the view of municipalities found in *MA 2001*. Section 2 of the Act states that municipalities are "responsible and accountable governments with respect to matters within their jurisdiction and each municipality is given powers and duties under this Act and many other Acts for the purpose of providing good government with respect to those matters." Section 8 of the Act states that "The powers of a municipality under this or any other Act shall be interpreted broadly so as to confer broad authority on the municipality to enable the municipality to govern its affairs as it considers appropriate and to enhance the municipality's ability to respond to municipal issues." We expect the approach to municipal budgeting to be one of a broad grant of powers to ensure municipal flexibility without being accompanied by narrow, new requirements that were not previously included in the Act.

Does not contribute to goal of long-term financial planning. The reporting requirements in the regulation do not contribute to the goal of encouraging municipalities to practice long-term financial planning. Our goal has been to encourage municipalities to ensure long-term sustainability with regard to operations, assets and growth while also building in allowances for various financial risks. Many of these concepts are dealt with very well in the MOE's **Toward Financially Sustainable Drinking-Water and Wastewater Systems (August 2007).** This is an approach we support and we have used materials from the Guide in our own training on full accrual budgeting and the move to long-term financial plans. However, the regulation requires a report that focuses on the expenses identified, including amortization. While these are important, they are not the only components of long-term sustainability, as the MOE financial planning guide notes. A report on amortization, post employment costs and post-closure costs is a long way from a long-term financial planning document. In the case where a municipality is funding the expenses in question, there is no need for a report. Yet it is impossible to conclude, for example, with regard to tangible capital assets, that the funding of amortization alone results in a sound asset management program. In fact, annual amortization may be quite small in relation to the full funding challenge associated with ensuring the eventual replacement or rehabilitation of major tangible capital assets. In short, the provisions of the regulation do not seem to achieve anything meaningful.

Part of a worrisome trend for a variety of reporting requirements. There is a growing requirement for reporting on assets through a range of statutes, regulations and funding programs. These requirements may be limited to a specific class of assets, and they may be broad or specific. We are concerned when Ministries continue to layer on new reporting requirements in a disjointed fashion that may vary from asset class to asset class and may still not meet the goal of ensuring long-term sustainability. Given that almost every municipality is subject to the requirement to undertake capital investment plans and community sustainability plans for a wide range of major assets under the federal gas tax program, it would seem that the additional reporting requirements in the regulation are unnecessary.

MFOA Recommendation:
Delete subsections 2, 3 and 4 of the draft regulation on budget matters.

If the Ministry is wedded to the existing language in the regulation, we suggest clarification that municipalities can base their reports to council on **estimates** for any of the three types of expenses that are not fully funded. If municipalities must base their reports to council on the expenses identified in audited financial statements, then budgets in 2010 and future years will be delayed significantly. In 2010, it could be July or later before a municipality has audited financial statements and a report to council that has been adopted by resolution. We feel that it would be useful to clarify that the report to council can be based on estimates of the expenses in question. We trust that there is no intention that this regulation changes the current *Municipal Act* provisions which allow a municipality to pass a budget in the year prior to the year to which the budget applies (with the exception of election years).

With regard to the content of a report, if a report is required, we would recommend broad language that allows municipalities to tailor a report to its needs and circumstances. The language in the current draft regulation probably embraces a significant range of reporting flexibility.

MFOA Recommendation:
Nothing in the regulation should force changes to the timing of municipal budget cycles or prevent municipalities from passing budgets early in a year or late in the prior year. Any reporting conditions should be broad and flexible to permit municipalities to tailor the report to their needs.

Debt and Financial Obligation Limit (amends O. Reg. 403/02 of the Municipal Act)

The regulation contains minor housekeeping amendments for O. Reg. 403/02. Generally these include:

- Eliminating references to “revenue fund” in favour of “revenues”
- Eliminating references to the capital fund
- Changing references to “expenditures” to expenses,” and
- Changing “capital undertaking” to “capital work.”

It is not clear that these changes are required as a result of the move to full accrual accounting. Nevertheless, MFOA has no objection to these changes.

<u>Bank Loans (amends O. Reg. 276/02 of the Municipal Act)</u>

Proposed amendments to O. Reg. 276/02 (Bank Loans) are housekeeping in nature and do not represent a policy change of any kind. We are not convinced that dropping the last part of the sentence in subsection 6(1) to eliminate the reference to expenditures was necessary, but the elimination of these words does not change the intent of the regulation. MFOA has no objections to this amendment.