



**STAFF REPORT  
ACTION REQUIRED**

**Toronto-York Spadina Subway Extension –  
Capital Funding Update**

<b>Date:</b>	May 20, 2008
<b>To:</b>	Executive Committee
<b>From:</b>	City Manager; Deputy City Manager and Chief Financial Officer; Chief General Manager, Toronto Transit Commission
<b>Wards:</b>	All
<b>Reference Number:</b>	P:\2008\Internal Services\SP\Ec08006SP (AFS#6088)

**SUMMARY**

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This report provides a capital funding update, and seeks authority to enter into a contribution agreement with the Federal Government, in relation to the Toronto Transit Commission (“TTC”): Toronto-York Spadina Subway Extension Project (“the Project”).

**RECOMMENDATIONS**

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The City Manager, Deputy City Manager and Chief Financial Officer, and the Chief General Manager of the Toronto Transit Commission recommend that:

1. Council authorize the City Manager, and the Deputy City Manager and Chief Financial Officer, in consultation with the Chief General Manager, Toronto Transit Commission and the City Solicitor, to negotiate on behalf of the City, a Building Canada Fund Contribution Agreement relating to the Toronto-York Spadina Subway Extension with the Federal Government of Canada and the Regional Municipality of York (“York Region”), in a form satisfactory to the City Solicitor, on terms and conditions as outlined in Appendix A to this report, and authorize execution of the Contribution Agreement by any of the City Clerk, Deputy City Manager and Chief Financial Officer, City Manager or Mayor, as appropriate.
2. In accordance with the terms of the proposed federal Contribution Agreement, Council direct the Deputy City Manager & Chief Financial Officer to apply the City’s share of investment

income, earned as of January 1, 2008, from the Move Ontario Trust towards Project capital costs.

3. Council direct the Deputy City Manager & Chief Financial Officer, to establish an obligatory reserve fund entitled “Toronto-York Spadina Subway Extension Working Capital Reserve Fund”, to be used for Project working capital purposes (as set out in more detail in Appendix B):
  - a. which reserve fund will be a repository for funds received from the Project’s funding partners on an ongoing basis and release payments to the TTC in order to facilitate the timely payment of invoices, with the funds to be held and invested in a manner consistent with Council policy, and all investment income to be applied to the Project;
  - b. which reserve fund would be administered by the Deputy City Manager and Chief Financial Officer; and
  - c. Municipal Code Chapter 227 (Reserves and Reserve Funds) be amended by adding the “Toronto-York Spadina Subway Extension Working Capital Reserve Fund” to schedule “15- Third Party Agreements Reserve Fund”.
  
4. Council direct the Deputy City Manager and Chief Financial Officer, and City Solicitor, in consultation with the Chief General Manager of the Toronto Transit Commission, to complete negotiations and finalize for execution by the City, a Project capital cost allocation agreement on behalf of the City with the Region of York, as previously directed, with amended terms and conditions in respect of the allocation of capital costs associated with the acquisition of aggregate property for the Spadina Subway Extension Project (“the Project”) as follows:
  - a. property acquisition shall be included as a Project component, forming part of the previously agreed-upon capital cost allocation structure of 59.96%City/40.04% York Region; and
  - b. any property acquired for the purposes of the Project which is subsequently declared to be surplus to the requirements of the Project shall be disposed of by the municipality which acquired it at no less than fair market value and the proceeds applied to Project capital costs or, if the books of the Project are closed, shared by the City and York Region according to the above-noted formula.
  
5. The appropriate City staff be authorized and directed to take all necessary actions, and that leave be granted for the introduction of any necessary bills in Council, to give effect thereto.

## **FINANCIAL IMPACT**

This report recommends that the City enter into a tri-partite contribution agreement with the Federal Government and with York Region for the purposes of securing up to \$622 million in federal funding for the Project (the “Contribution Agreement”). It is important to note that costs become eligible for federal reimbursement only after the Contribution Agreement is signed.

The total Project capital cost was originally estimated at \$2.1 billion (expressed in 2006 dollars). However, including inflationary impacts, the capital cost is now estimated at \$2.6 billion (nominal dollars). The Province has recently provided an additional \$200 million towards Project capital costs, thereby increasing the total Provincial capital funding to \$870 million, held in the Move Ontario Trust (the “Trust”). With the addition of Trust investment income as recommended in this report and upon the signing of the federal Contribution Agreement the Project is now considered to be fully funded by the City, York Region, and the federal and provincial governments. The resultant funding, by partner, may be summarized as follows:

Funding Partner:	\$ millions	% of funding
Federal	\$697	26.5%
Provincial	\$1,059*	40.2%
Municipal	\$878	33.3%
Total	\$2,634	100.0%

\*including investment income

## DECISION HISTORY

### Capital Cost Allocation

At its meeting of September 25, 26, 27, 2006, City Council adopted recommendations of Policy and Finance Committee Report No 7, Clause 35,  
<http://www.toronto.ca/legdocs/2006/agendas/council/cc060925/pof7rpt/cl035.pdf>

including the determination of a municipal capital cost allocation formula for the Project, reflecting a cost sharing of 59.96 % City/ 40.04 % York Region.

One exception, as noted in the report, was that \$100 million was to be set aside for property acquisition, with the cost to be borne directly by the municipality having jurisdiction over the property to be acquired.

### Project Governance and Ownership

At its meeting of May 23, 24, 25, 2007, City Council adopted recommendations of Executive Committee Report No 8.5  
<http://www.toronto.ca/legdocs/mmis/2007/ex/reports/2007-04-30-ex08-cr.pdf>

authorizing a set of principles for an Operating Memorandum of Understanding between the City, TTC, and York Region, that included TTC ownership of, and responsibility for, the subway extension infrastructure, its operations, maintenance, and regulation.

In recognition of the shared municipal financial interests associated with Project delivery (i.e. capital construction), the recommendations also included a project delivery structure, which incorporated the following:

- the TTC as Project Manager; and
- an “Oversight Task Force”, comprised of senior municipal staff, mandated to perform a Project oversight function in order to ensure Project delivery in accordance with Council directions, and to serve as Project liaison to Councils/Committees of both the City and York Region. Subsequent to reporting in May 2007, the task force was renamed the “Executive Task Force” (ETF).

## **Federal Contribution**

In September 2006, City Council adopted a recommendation, setting as a condition precedent for the Project the receipt of a Federal government funding commitment for one-third of the Project capital cost.

On March 6, 2007, Prime Minister Stephen Harper pledged up to \$697-million towards eligible Project costs, with receipt of the funds conditional upon completion of a due diligence review, the negotiation of a contribution agreement, and adherence to conditions that were to be put forth by the Federal Ministers of Finance, and of Transport, Infrastructure and Communities.

Subsequently, in May 2007, Council adopted a recommendation directing that: “the capital contribution from the City not exceed its share (59.96%) of the one-third funding that would be attributable to the municipal sector, and that a request be made to the Provincial and Federal Governments to provide a full two-thirds funding of actual Project capital costs.”

## **Provincial Funding**

As part of the Ontario Budget, on March 23, 2006, the Province announced the creation of “Move Ontario”, for the purpose of investing in public transit, municipal roads and bridges, including allocation of \$670 million to assist in funding Project capital costs. These funds were deposited into the Move Ontario Trust (“the Trust”), which was created for the specific purpose of holding the Provincial funds.

All funds held in the Trust are invested in interest-earning vehicles. However, as the Trust is a taxable entity, the interest earnings are paid out to the municipal stakeholders on an annual basis. Of the investment earnings received from the Trust by the City in fiscal 2006 and 2007, a total of \$30 million was recorded in the City’s operating budgets, and \$2.9 million was deposited into the Strategic Infrastructure Partnership Reserve Fund, created by Council at its meeting of July 25, 26, 27, 2006.

## **ISSUE BACKGROUND**

This report provides a capital funding update, and seeks authority to enter into a Contribution Agreement with the Federal Government required for the purposes of receiving the remainder of the Project funding.

Additionally, in order to achieve full Project capital funding, this report recommends that interest earnings that are related to the capital funding currently held in Trust be applied towards Project costs.

## **COMMENTS**

### **Subsequent Funding Events**

Subsequent to its funding pledge of up to \$697 million, the Federal Government provided an up-front payment of \$75 million, attributed under the Public Transit Capital Trust, which was deposited into the (Move Ontario) Trust.

In December 2007, the Province pledged an additional \$200 million towards Project capital costs, which has also been deposited into the Trust.

### **Federal Requirements**

The federal announcement indicated that the funding of up to \$697 million would become available, to be received upon completion of a due diligence review, and negotiation of a Contribution Agreement between the Federal Government, the City, TTC, and York Region, which would include conditions put forth by the Federal Ministers of Finance, and of Transport, Infrastructure and Communities. As the federal government subsequently provided an advance of \$75 million towards the Project, the due diligence process only relates to receipt of the remaining \$622 million.

The federal funding will be received through the Building Canada Fund (BCF), a successor to the Canada Strategic Infrastructure Fund, the framework for which was finalized by Treasury Board in November 2007.

#### **1. Requisite Approvals**

In February 2008, staff of the City, TTC, York Region, and the Province (together, “the Applicants”) collaborated on, and submitted a BCF application report to the federal government for the purposes of the Project being considered by Treasury Board for funding approval. The application incorporated input that was received from federal staff during the drafting stages. We are advised that federal staff will be bringing the report before Treasury Board in late May 2008, and that the requisite federal approvals will be received shortly thereafter.

In addition, as a prerequisite to receiving funding, the Project is required to receive Federal Environmental Assessment (EA) approvals under Canadian Environmental Assessment Act (CEAA). To that end, City/TTC/York Region staff submitted the requisite reports to Transport Canada (the “Federal Responsible Authority” for this EA), following which approvals were received in March 2008.

## 2. Fully Funded Project

The Federal BCF application gave rise to an immediate requirement for the municipalities to demonstrate that the Project is fully funded, giving consideration to a maximum total federal contribution of \$697 million. However, the federal commitment was based on an original total Project capital cost estimate of \$2.1 billion (expressed in 2006 dollars). As a result inflationary impacts, the capital cost is now estimated at \$2.6 billion (nominal dollars).

In order to demonstrate that the Project is fully funded, while ensuring that the funding provided by the municipal partners will not exceed one-third of Project capital costs, in accordance with previous Council direction:

- the Province deposited an additional \$200 million into the Trust;
- it will be necessary to apply all of the investment income generated by the funds held in the Trust towards Project capital costs. This is also a requirement under the proposed federal Contribution Agreement (see Appendix A), as outlined in more detail below; and
- in order to enhance the Trust’s potential for generating investment income, federal staff have agreed to contribute funds in a higher proportion (i.e. of total annual funding) during the early project years as compared to the later years.

This report recommends, in accordance with the terms of the proposed federal Contribution Agreement, that all income earned and received by the City from the Trust, retroactive to January 1, 2008, be applied solely towards the funding of Project capital costs.

## 3. Public-Private Partnerships (“P3”)

A requirement of the BCF application was that it include a review of potential P3 options for Project delivery, giving consideration to federal interim guidelines as provided to the Applicants by federal staff. In order to address this requirement, the Applicants retained outside consulting expertise to undertake a preliminary P3 screening.

Applicable P3 options would allow the TTC to continue as Project Manager, and as owner and operator of the subway extension, in accordance with previous Council direction. As a result, the possible P3 options identified by the consultants included those relating to the design, build, and potential financing of the infrastructure, and excluded those involving any potential outsourcing of operations or maintenance.

Although an important exercise, this analysis is considered to be preliminary, given that the TTC has yet to undertake the detailed Project engineering and design phase, which will commence only once project staffing is in place. The Contribution Agreement acknowledges that the P3 screening undertaken was preliminary, and requires that the TTC/City/York Region continue to

consider the potential P3 options and deliver a final P3 screen for specific Project components to the federal government (see Appendix A). The TTC will undertake this exercise using a value engineering approach.

The TTC, in consultation with municipal staff, will give consideration to the results of the P3 screening in developing a project delivery strategy once more detailed information becomes available. The recommended project delivery strategy will then be submitted to the Executive Task Force and the (TTC) Commission for approval.

#### 4. Federal Contribution Agreement

In order to receive the balance of the federal funding commitment of \$622 million, under the BCF program, the City and York Region are required to enter into a Contribution Agreement with the federal government, while at the same time, the Province is first required to enter into a separate framework agreement with the federal government.

The purpose of the Contribution Agreement is to establish the terms and conditions under which the federal government would reimburse the City and York Region for a portion of Project capital costs. The principles of the Contribution Agreement are set out in Appendix A to this report.

It is important to note that certain categories of costs are considered to be ineligible for federal reimbursement, including land acquisition costs, financing charges and costs incurred prior to the signing of the Contribution Agreement. Eligible costs incurred are recoverable only after invoices are paid.

This report recommends that the appropriate senior staff be authorized to negotiate and execute a Contribution Agreement, in a form satisfactory to the City Solicitor, on terms and conditions as outlined in Appendix A.

#### **Flow of Funds**

Given the complexity of administering a payment process for a project of this magnitude with multiple funding partners, the City, TTC, and York Region staff have agreed to follow current TTC/City payment administration practices and procedures for similar TTC capital projects. This would allow the Project to benefit from using existing internal expertise, and standardized practices and procedures, thereby allowing for the timely processing and payment of project invoices, allowing for the timely submission of claims to funding partners, and enhancing the Project Manager's ability to prepare the required Project reporting in an efficient manner.

Therefore, under the agreed-upon arrangement:

- the TTC (as Project Manager) will assume responsibility for receiving, verifying, and paying contractor invoices, preparing detailed financial reporting, and preparing funding claims to the various funding partners; and
- the City will assume responsibility for receiving funding from the various partners, submitting funding claims to the various partners, managing working capital, and ensuring

that the funds are available for application towards invoice payments and managing working capital interest income and reserve fund reporting.

In order to ensure the timely payment of invoices, it will be necessary to set aside a pool of funds, on an ongoing basis, for working capital purposes. Depending on the availability of capital over the life of the Project, the funds may be received from one or more of the Project's funding partners. However, subject to the concurrence of the Trustees of the Trust, the Trust would provide the necessary funds at the outset.

When not in use, the working capital funds would be temporarily invested, with the investment income applied to the Project. As the City will be responsible for managing the working capital funds, this report recommends that:

- a working capital reserve fund be established as an obligatory reserve fund with criteria as set out in Appendix B;
- the working capital reserve fund be invested (when the funds are temporarily not in use) in a manner consistent with the investment policy applicable to reserve accounts, adopted by City of Toronto Council at its meeting of March 3, 2008  
<http://www.toronto.ca/legdocs/mmis/2008/ex/reports/2008-02-06-ex17-cr.pdf>

## **Property Capital Cost Allocation**

Council previously approved a municipal Project capital cost allocation of 59.96 % City/ 40.04 % York Region. However, property acquisition costs were excluded from the formula, which were to be borne directly by the municipality having jurisdiction, with \$100 million having been set aside in aggregate.

City and York Region staff have continued to engage in Project-related negotiations, and have determined that it would be preferable to view all property acquisition, regardless of geographic location, in the same manner as all of the other Project components. Accordingly, this report recommends that property acquisition be included as a Project component, forming part of the overall capital cost allocation structure as previously agreed upon (i.e. 59.96% City/40.04% York). This would allow for a shared responsibility for the property acquisition budget, and for the application of any surplus of property acquisition funds to be applied towards overall Project capital costs under the same overall formula.



This report further recommends that in the event that any land is determined to be surplus to the Project, it would be disposed of at no less than fair market value, with the proceeds applied to Project capital costs. Should such disposal occur after the Project books are closed, the proceeds would be returned to the municipalities in proportion to the municipal Project capital cost allocation of 59.96 % City/ 40.04 % York Region.

## CONTACTS

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## SIGNATURES

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Shirley Hoy  
City Manager

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Gary Webster  
Chief General Manager  
Toronto Transit Commission

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Joseph P. Pennachetti  
Deputy City Manager and  
Chief Financial Officer

## ATTACHMENTS

Appendix A – Federal Contribution Agreement - Principles  
Appendix B - Toronto-York Spadina Subway Extension - Working Capital Reserve Fund

## Appendix A Federal Contribution Agreement- Principles

Purpose of the federal Contribution Agreement as between Canada, the City and York Region (“the Contribution Agreement”)

1. to establish terms and conditions under which the federal government (“Canada”) will reimburse the City and York Region (together, “the Recipients”) for a portion of the Project costs

Term

2. effective from the date that the Contribution Agreement is signed to March 31, 2017, subject to early terminations rights of Canada in the event of a default by the Recipients

Federal Commitment

3. Canada will contribute up to one-third (1/3) of Eligible Costs of the Project, as of the date of signing of the Contribution Agreement, up to a total of \$622 million, subject to
  - there being an appropriation by parliament for the fiscal year in which the payment is to be made
  - funding may be reduced or terminated in response to Canada’s annual budget, or a parliamentary spending decision that has an impact on the program under which this agreement is made
  - Canada’s total financial assistance (from all sources, including the Contribution Agreement) to the Project may not exceed fifty percent (50%) of total Eligible Costs. Under this circumstance, Canada may reduce, or recover an amount equal to the excess
  - total financial assistance received by the Recipients for the Project from all sources may not exceed 100% of total Eligible Costs. Under this circumstance, Canada may reduce, or recover an amount equal to the excess
  - payment will be subject to a five percent (5%) holdback for each Project component until the completion of the Project component
4. Eligible Costs are Project costs eligible for reimbursement under the Contribution Agreement and are defined as “all necessary direct costs incurred properly and reasonably for the implementation of the Project”, including:
  - capital costs of acquiring, constructing or renovating a tangible capital asset
  - costs of joint communication activities and road signage recognition
  - costs of project-related signage, lighting, project markings, and utility adjustments
  - planning and assessment costs such as the costs of environmental planning, surveying, engineering, architectural supervision, testing and management consulting services
  - costs of engineering and environmental reviews, including environmental assessments and follow-up programs as defined in the Canadian Environmental Assessment Act and the costs of remedial activities, mitigation measures and follow-up identified in any environmental assessment
  - costs of developing and implementing innovative techniques for carrying out the Project
  - audit and evaluation costs as specified in the Contribution Agreement

- other costs that are direct and necessary for the successful implementation of the Project, in the opinion of the Federal Government, and which are approved by the Management Committee set up under the Contribution Agreement
5. Ineligible Costs are Project costs which are not eligible for reimbursement under the Agreement, and include:
- costs incurred after the Project completion date
  - costs incurred prior to signing the Contribution Agreement
  - sole source contracts
  - costs of land acquisition (and associated fees), leasing land, buildings, equipment and other facilities
  - costs of general repairs and maintenance of Project work and related structures, unless they are part of a larger capital expansion Project
  - costs of services or works normally provided by the Recipients, incurred in the course of implementation of the Project
  - costs of any goods and services which are received through donations or in kind
  - internal employee wages and benefits, overhead costs as well as other direct or indirect operating, maintenance and administrative costs, relating to services delivered directly by permanent employees of the Recipients or of a corporation owned and controlled by the Recipients
  - costs of developing and implementing a Transit Demand Plan and associated measures
  - cost of developing a business case or proposal for funding
  - financing and interest charges on loans
  - legal fees
  - sales taxes

#### Management Committee

6. comprised of representatives from both Canada and the Recipients
7. established to monitor the progress of the Project, and administer, manage, and enforce the provisions of the Agreement
8. all recommendations and decisions of the Management Committee must be unanimous

#### Municipal Responsibilities

9. to fund all Project costs, including cost overruns, and seek reimbursement from Canada in respect of Eligible Costs
10. to implement the Project in accordance with the terms and conditions of the Contribution Agreement
11. to use the Province of Ontario's contributions, held in the Move Ontario Trust, plus any interest earnings after January 1, 2008, solely and exclusively for the Project
12. to disclose all financial assistance received for the Project
13. in the event that there are cost over-runs in comparison to anticipated costs, to provide Canada with a summary of measures proposed to remedy the shortfall to Canada's satisfaction so as to avoid suspension of payments under the Agreement by Canada and/or declaration of default under the Agreement by Canada
14. to comply with environmental assessment obligations as per the Canadian Environmental Assessment Act (CEAA) report

15. to provide a Transportation and Demand Management plan that meets federal requirements to the Management Committee by June 30, 2013
16. within twelve (12) months, to provide Canada with an independent and objective Final P3 Screen and delivery strategy for specific Project Components that is consistent with the previously submitted Preliminary P3 screen and Federal guidelines.
17. to award and manage all Contracts in accordance with relevant policies and procedures, and to ensure all Contracts are awarded in a way that is transparent, competitive and consistent with value for money principles and is in accordance with the Agreement on Internal Trade, or in a way that is otherwise acceptable to Canada
18. to prepare and make available all documentation required under the Agreement, including payment claim forms, approval documents, Contracts, financial forecasts, status reports
19. to ensure that any audit requested by Canada is performed and to provide, upon request, accurate and timely financial forecasts and status reports

#### Events of Default

20. the Recipients will be in default under the Contribution Agreement if they have submitted false or misleading information or made false or misleading representations to Canada, have not complied with any condition, undertaking or term of the Contribution Agreement, have neglected or failed to pay to Canada any amount due in accordance with the Contribution Agreement or Canada has determined that they are unable to complete construction of the Project unless they expend in excess of the funding available to them.

#### Remedies available to Canada

21. if upon receipt of written notice, the Recipients fails to remedy a breach to Canada's satisfaction after 30 days, Canada may suspend payment, may declare the Recipients to be in default of the Agreement, may terminate the Agreement, and may require reimbursement of all or a portion of its contribution, with interest
22. if, over a 25 year period, the Recipients dispose of, or essentially abandon the subway extension assets, or render them unavailable for public use, then Canada will require reimbursement of its contribution in a declining proportion. An exception is made if the assets are transferred between Toronto and York for nominal consideration within a pre-established time period

#### Indemnity

23. The Recipients indemnify Canada, etc.(its officers, servants, employees or agents) from and against any harm arising from the Project (including the design, construction, operation, maintenance and repair of any part of it), the performance of the Agreement, and any omission or wilful or negligent act of the Recipients or a third party, with the exception of any act or negligence of Canada, etc. in the performance of his or her duties.

Appendix B  
Toronto-York Spadina Subway Extension:  
Working Capital Reserve Fund

(a) Location within the Consolidated Reserve Fund Schedule

Account within Schedule #15 – Third Party Agreements Reserve Fund

(b) Statement of Purpose

The Toronto-York Spadina Subway Extension Working Capital Reserve Fund will be a repository for funds received from the City, York Region, the Province of Ontario, and/or the federal government of Canada for the purposes of the Toronto-York Spadina Subway Extension Project (“the Project”), which funds will be deemed to be required for Project working capital purposes.

(c) Service Area or Beneficiary Program:

Toronto Transit Commission

(d) Contribution Policy:

The funding partners noted in (b) above will contribute funds to the Project, which will be deposited into the reserve fund account on an ongoing basis, in an amount that will be determined through continued preparation and review of Project requirements, and with the funds held to be invested in a manner consistent with Council policy, and all investment income to be applied to the Project.

(e) Withdrawal Policy:

Funds will be withdrawn from the reserve fund to be applied as source funding for the TTC capital expenditures on the Toronto-York Spadina Subway Extension Project and as consistent with the City’s normal capital budget processes.

(f) Review Cycle:

The Toronto-York Spadina Subway Extension Working Capital Reserve Fund will cease to exist after payment of the final Project invoice by the TTC, after which, the reserve fund will be depleted by paying any remaining funds back into the Project, and then closed.