Town of Whitchurch-Stouffville Council Report Item 8.5

Subject:	**Pay-on-Demand Surety Bond and Letter of Credit Policies**
Staff Report No.	**FI-002-25**
Department/ Commission:	**Finance Services Commission**
Date:	**March 19, 2025**

Recommendation:

1) That Council receives the report entitled "Pay-on-Demand Surety Bond and Letter of Credit Policies."

2) That Council approves the Pay-on-Demand Surety Bond Policy as set out in Attachment 1.

3) That Council approves the Letter of Credit Policy as set out in Attachment 2.

Report Highlights

- A new provincial regulation under section 70.3.1 of the Planning Act, introduced on November 20, 2024, permits the use of Surety Bonds for securing public infrastructure construction, enabling developers to release capital for additional home-building projects.
- The regulatory framework ensures the reliability of Surety Bonds through licensing, credit rating requirements, guaranteed and timely payments, partial drawdowns, and cancellation provisions.
- Pay-on-Demand Surety Bond policy is being brought forward by staff. The policy aligns with the Town's housing objectives and is modeled after similar policies from other municipalities, promoting development while maintaining financial security.
- The Letter of Credit Policy is also being brought forward by staff. This policy will formalize the existing process and guidelines for the acceptance, management, and administration of Letters of Credit collected by the Town.

1. Purpose:

This report seeks Council approval for the adoption of a Pay-on-Demand Surety Bond Policy. The policy will allow infrastructure works required through development agreements (subdivision and site plans) to be secured by Pay-on-Demand Surety Bonds, either as an alternative or in addition to the customary Letter of Credit.

Furthermore, this report requests Council approval for the adoption of a Letter of Credit Policy. While the Town has established guidelines for accepting and managing Letter of Credits, no official policy is in place.

2. Background:

The Town of Whitchurch-Stouffville requires developers to provide financial security, typically in the form of Letters of Credit or cash, to ensure they meet their development agreement obligations. On November 20, 2024, a new provincial regulation under section 70.3.1 of the Planning Act was introduced which allowed the use of surety bonds as an acceptable financial instrument for securing public infrastructure construction through development agreements. The regulation aimed to enable developers to release capital that would have been tied up in Letters of Credit, allowing it to be invested in additional home-building projects to support the provincial housing mandate.

A Pay-on-Demand Surety bond is a three-party agreement involving the developer, the Town, and the insurer. It guarantees that the insurer will pay the Town if the developer fails to fulfill their obligations.

A Letter of Credit is a document issued by a financial institution on behalf of its customer, authorizing the Town to receive an amount up to the stipulated value in the Letter of Credit if the customer defaults on a contractual obligation with the Town. The Town follows established guidelines for its Letter of Credit process. A standardized Letter of Credit format is used, outlining acceptable wording, financial institution requirements, and other conditions.

The regulation does not require developers and municipalities to use Pay-on-Demand Surety Bonds. However, if a developer chooses to provide it to secure municipal land-use planning obligations, then a municipality would be required to accept this instrument as a financial assurance with the instrument having certain mandatory features as set out in the regulation.

On April 20, 2021, Council approved the acceptance of a Pay-on-Demand Surety Bond from Far Sight Investments Limited for Application SPA20.009, making the Town one of the first municipalities in York Region to adopt this instrument before the provincial regulation was in place.

3. Analysis:

3.1 Pay-on-Demand Surety Bond

In November 2024, the Province adopted a regulatory framework under Section 70.3.1 of the Planning Act to guide the use of Pay-on-Demand Surety Bonds. This framework includes specific elements to ensure these bonds are secure and reliable, making them a suitable alternative or supplement to Letters of Credit for municipalities.

These elements are summarized in the table below:

Table 1: Mandatory elements of Pay-on-Demand Surety Bonds

Element	Details	Staff Comments
Licensing Requirement	Issued by an insurer licensed under the Insurance Act and overseen by the Financial Services Regulatory Authority of Ontario.	Regulation ensures that only qualified and regulated insurers can issue these bonds, adding a layer of security.
Credit Ratings Requirement	Insurer must meet one of the following credit ratings: • Dominion Bond Rating Service: “A” or higher • Fitch Ratings: “A-” or higher • Moody’s Investors Service Inc.: “A3” or higher • Standard and Poor’s: “A-” or higher • A.M. Best Company, Inc.: “A” or higher.	Credit ratings provide an independent assessment of the insurer's financial stability and ability to fulfill obligations.
Guaranteed Payment	Insurer guarantees payment to the municipality if the developer defaults on their obligations.	Ensures that the municipality can rely on the bond to secure funds needed to rectify any defaults.
Timely Payment	Insurer must make payment to the municipality within 15 business days of receiving a written notice of default.	Guarantees quick access to necessary funds for the municipality to address any issues.
Partial Reductions	Allows for partial drawdowns, similar to Letters of Credit, enabling the municipality to release or reduce the security amount as conditions are met.	Provides flexibility for the municipality to adjust the security amount as the developer meets conditions.
Cancellation	Insurer must provide a written notice to the municipality and the developer at least 90 days in advance of terminating the surety bond. Developer must provide replacement security within 60 days of receiving the notice, or the existing bond remains in force.	Ensures continuous security for municipal obligations, with safeguards in place if no replacement is provided.

These measures collectively ensure that surety bonds are a reliable and secure financial instrument for municipalities. Staff are confident that Pay-on-Demand Surety Bonds will offer the same level of security and immediate financial protection as currently provided by Letters of Credit, while helping to facilitate development.

3.2 Letters of Credit

The Town has historically accepted Letters of Credit as a form of security and follows established guidelines utilizing a standardized Letter of Credit format that specifies acceptable wording and conditions. This format is an integral part of the agreements included as Schedule ”D”. Under the agreement, the counterparty provides securities to the Town in the form of cash, a certified cheque, a bank draft or a Letter of Credit. The agreement also outlines the conditions for reducing or releasing securities, the process for drawing on them when necessary, and the requirements for replenishing them to their full original value.

When a Letter of Credit is chosen as a form of security, The Finance Commission verifies the amount in accordance with the agreement and ensures that the wording, terms and conditions comply with the required standards. Once the obligations of the agreement are met, staff initiate requests for reductions or releases of the securities, which are then directed to the Treasurer for processing.

The Letter of Credit policy that is being brought forward aims to establish a consistent and streamlined approach across the Town, ensuring clear procedures and a defined approval framework.

The current Letter of Credit format has been updated and can be found in Appendix A of Attachment 2 to this report. The format will ensure that all pertinent and required information is included to assist staff in the administration of the securities.

3.2 Comparison of Security Options

There are distinctions between the two instruments discussed above. The features are summarized in the comparison table below.

Table 2: Comparison of Security Options

	Letter of Credit	**Pay-On-Demand Surety Bond**
Issuer	Schedule 1 Chartered Bank or other authorized Financial Institution	Licensed Insurance Company
Regulation	Office of the Superintendent of Financial Institutions	Office of the Superintendent of Financial Institutions
Financial Ratings	S&P, Moody’s and DBRS	S&P, Moody’s, DBRS, Fitch, A.M Best

Proof of Loss	Pay-on demand to the financial institution. Not required to prove the default	Pay-on-demand letter provided to surety. Not required to prove the default
Payment Timelines	Silent of timeline, but typically 1-3 business days	15 days
Credit Type	Secured; bank will retain security to cover the risk	Unsecured credit; unregistered general indemnity
Prequalification	No prequalification and provides no insight to capabilities	Surety will review the financial position as well as the experience and resources needed to deliver on the underlying obligations
Benefit	Amount is applied to operating loan facility	Does ***not*** tie up developer's liquidity or borrowing power

4. Options:

To facilitate development and support the Town's housing objectives, Town staff have prepared a Pay-on-Demand Surety Bond Policy (Attachment 1). This policy enables the use of Surety Bonds as an alternative or supplement to Letters of Credit where appropriate. Provincial regulation serves as the overarching framework for using these bonds to secure the construction of on-site/municipal services required by subdivision and site plan approvals and agreements. The policy aligns with the Town's Letters of Credit policy (Attachment 2) and is modeled after policies from neighbouring municipalities that have adopted similar changes to their development finance framework. An Agreement template for the Surety Bonds instrument is included as Appendix A of the policy.

Surety Bonds will not be used to secure development charge payments and are not expected to be used for smaller security obligations related to construction, such as in-fill housing and pool construction. Letters of Credit will continue to be used for these obligations.

The Town will not exchange Letters of Credit issued prior to the enactment of the Pay-on-Demand Surety Bond Policy for Surety Bonds.

This report also formalizes a Letter of Credit policy. Implementing a formal policy along with an established standard template will streamline the process for both Town staff and external parties and enhance service delivery.

The Policy will apply to all Letters of Credit requested by the Town from the date the Policy is enacted. If a Letter of Credit was requested before the Policy was enacted, it will be executed according to previous operating practices and held by the Finance Commission until its renewal, expiry, or draw date, whichever occurs first. Except for automatic renewals, any Letter of Credit requiring renewal or reissuance will be subject to the terms outlined in the new Policy.

5. Financial Implications:

There is no financial impact on the Town. The mandatory elements outlined in the regulation ensure the reliability of this financial instrument, resulting in unchanged risk assumed by the Town.

6. Broader Intergovernmental Impacts and/or Considerations:

Pay-in-demand Surety Bond Policy will promote development and align with the Town's housing objectives as well as the Provincial housing mandate.

7. Communication:

N/A

8. Alignment with Strategic Plan:

1. A Town that Grows
   A Town that grows in support of complete communities

2. Organizational Effectiveness
   To Elevate our Organizational Effectiveness

9. Attachments:

Attachment No. 1 – Pay-on-Demand Surety Bond Policy
Attachment No. 2 – Letter of Credit Policy

10. Related Reports:

FTS-008-21 "Acceptance of Pay-On-Demand Subdivision Bonds", April 20, 2021

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