

<b>TO:</b>	<b>CHAIR AND MEMBERS CIVIC WORKS COMMITTEE MEETING ON APRIL 2, 2012</b>
<b>FROM:</b>	<b>JOHN BRAAM, P. Eng. ACTING EXECUTIVE DIRECTOR, PLANNING, ENVIRONMENTAL &amp; ENGINEERING SERVICES &amp; CITY ENGINEER</b>
<b>SUBJECT:</b>	<b>FIXED RATE FOR WATER AND SANITARY CHARGES</b>

<b>RECOMMENDATION</b>
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That, on the recommendation of the Acting Executive Director, Planning, Environmental & Engineering Services & City Engineer, for the City of London the following actions **BE TAKEN**:

- a) Administration **BE DIRECTED** to proceed with preparation of a by-law to implement Phase 1 of the fixed rate charge for water and sanitary servicing which is more representative of the fixed costs related to billing and infrastructure renewal than the current structure;
- b) Administration **BE DIRECTED** to inform stakeholders on the need for the structural changes to the rates, the rationale for the charge and the potential impact on customers;
- c) Administration **BE DIRECTED** to hold a public meeting before Committee for the purpose of passing a by-law to authorize a structural change to fixed charges for water and sanitary rates for implementation in 2012.

It **BEING NOTED**, the structural change will be revenue neutral and no additional revenues will be realized in the 2012 budget year.

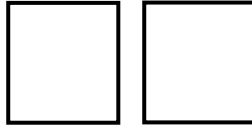
It **BEING FURTHER NOTED**, this is this first phase of changes to the rate structures and additional changes, as previously presented, will be brought before Committee and Council in late 2012 as part of Phase 2.

<b>PREVIOUS REPORTS PERTINENT TO THIS MATTER</b>
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The reports noted below can be found at:

<http://www.london.ca/d.aspx?s=/Meetings/Default/meetingpackages.htm>

- [Water, Sanitary and Storm Rate Structure Review - Fixed Rate for Water and Sanitary Charges, August 15, 2011, Built and Natural Environment Committee, Agenda Item # 7;](#)
- [Council Proceedings 14th Meeting, July 26, 2010 – page 30](#)
- [Presentation by Administration, London Economic Development Committee and Industry representatives from AB In Bev \(Labatt\) and Casco at July 19th meeting of ETC](#)
- [Water, Sanitary and Storm Rate Structure Review – Update on Implementation Timing and Consultation Process, July 19, 2010, Environment and Transportation Committee, Agenda Item # 26a, deferred from June 21, 2010](#)
- Council Proceedings 15<sup>th</sup> Meeting, July 27, 2009 – Item 285, 14<sup>th</sup> Report of the Board of Control, Clause #9, as amended;
- Water, Sanitary and Storm Rate Structure Review – Update on Implementation Timing, July 20, 2009, Environment and Transportation Committee, Agenda Item # 5;
- Sewer Surcharge of Water Used to Water Lawns, Flower Beds and Swimming Pools, January 12, 2009 – 2<sup>nd</sup> Report of the Environment and Transportation Committee, Item #19 and Agenda Item #17;
- Council Proceedings 15<sup>th</sup> Meeting, July 21, 2008 – Item 241, 22<sup>nd</sup> Report of the Board of Control, Clause #26, as amended;
- Water, Sanitary and Storm Rate Structure Review – Revisions to Current Structure, July 16, 2008 – 22<sup>nd</sup> Report of the Board of Control, Item #26 and Agenda Item #33;
- Water, Sanitary and Storm Rate Structure Review – Update on Concerns coming out of Consultation Process, May 28, 2008 – 17<sup>th</sup> Report of the Board of Control, Item #20 and



Agenda Item #24;

- Water, Sanitary and Storm Rate Structure Review – Update Report, May 7, 2008, Board of Control, Agenda Item # 7;
- Water, Sanitary and Storm Rate Structure Review – Update on Concerns coming out of Consultation Process, November 14, 2007 – 31<sup>st</sup> Report of the Board of Control, Item #30 and Agenda Item #5;
- Water, Sanitary and Storm Rate Structure Review – Update on Consultation Process, August 8, 2007, Board of Control, Agenda Item # 25(a) and R. Jawniuk et al – Petition re: Storm Sewer Charges – Selkirk Street and Braesyde Avenue, Agenda Item # 25(b);
- Erosion and Sediment Control Requirements and Practices for Construction Sites to Ensure Water Quality Protection for Open Watercourses, June 18, 2007, Joint Environment and Transportation Committee and Planning Committee, Agenda Item #12;
- Several previous reports were referenced in the August 8, 2007 Board of Control Report.

<b>BACKGROUND</b>
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**Purpose**

Administration is seeking Council’s approval to introduce stability into rate setting for the water and sanitary utilities by including a fixed charge more reflective of the revenues needed to address life cycle infrastructure renewal. Inclusion of a larger fixed charge will ensure the utilities move towards a more financially sustainable position in consideration of declining consumption.

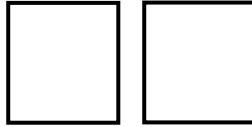
**Background**

The water and wastewater systems are customer owned and supported utilities. Water and sewer rate charges provide the revenue streams needed to sustain these utilities. City staff undertake the stewardship roles to ensure the utilities are well managed and maintained for current and future generations. Total revenues for the two utilities are approximately \$130,000,000. Customer charges are based on formulae depending on the type of customer (aggregated into classes), their water consumption, sanitary sewage generated and land area of their property. The current rate structure was established more than 22 years ago for water and 15 years ago for sanitary rates. It has been identified as being one of the most complex rate structures in Ontario and contains inequities between customer classes and lacks consistency between the water and sewer customer classes and rate structures.

In 2004, Administration began a review of the water, sanitary and storm rate structures, in an effort to simplify the structure and improve fairness. Since then, the review has undergone several iterations in response to requests by the City’s elected officials and our stakeholders. While the process undertaken was well received and the most recently suggested rate structures are recognized as improving the fairness and equity, the current economic conditions have lead Council to avoid changes which might adversely affect employment retention and our competitive advantage to attract new businesses. In 2010, Council once again deferred the implementation of the proposed rate change and also requested whether simpler options might be available and to address the concerns of high volume industrial users.

**Discussion**

Over the past few years, while attempting to implement the new rate model, the conservation efforts by our customers have become more significant as they recognize that the consumer has ultimate control of how much is paid for water and sanitary services by simply reducing consumption. The resulting impact on water and sewer revenues has been significant both in London and many other municipalities across North America. Numerous municipalities have altered their rate structures by increasing the portion of their bill that is fixed month to month to improve revenue stability and long term sustainability. The BMA Municipal Study 2010 has identified that of the 83 municipalities surveyed, 77 percent include a fixed rate from 1% to 88% of a typical monthly bill. This Benchmarking table was updated in 2011 and is included as Appendix B in BMA’s summary report. London is currently at the low end of the scale with a minor fixed charge of 1.7% and no sanitary fixed



charged. There is however a minimum charge of \$5 per month if water consumption is lower than 3 cubic metres per month.

Administration is recommending that, in the phase 1 implementation, a fixed rate charge for water and sanitary be implemented that would cover a portion of the capital cost requirements to support pay-as-you-go financing for system renewal. Fire protection charges are currently not separately identified and it is recognized that low volume users do not adequately contribute to the infrastructure required to provide fire protection. Fixed charges would also cover meter reading, billing, meter renewal and customer billing charges. The proposed fixed charge would be identified on the water and sewer bill as an infrastructure renewal charge.

This change is proposed as phase 1 for implementation in 2012. The new fixed charges would be revenue neutral, thereby not impacting business budget setting in the short term. In fact many of the large water customers may see a decline in their overall water and sewer bill.

To assist the City with this review, BMA Management Consultants were hired. They have undertaken all of the previous rate structure reviews and have a very strong understanding of the rate structures of other municipalities across Ontario from the annual Municipal Report which they author. Their summary report is attached as Appendix "A". They have identified that fixed expenditures for London are in the range of 60 to 80 percent. They have recommended that a fixed charge for both water and sanitary be phased in that would recover 30 percent of the rate based expenditures. The fixed charge could be increased to reflect an amount closer to the 60 percent when the full rate structure review is re-visited later this year for Phase 2 implementation in 2013.

Goals and Objectives of Modified Rate Structure

In previous reports to Committee and Council, our principles were articulated for consideration in evaluating and selecting the most desirable rate structure. BMA has simplified these to six:

1. Revenue Stability
2. Fairness & Equity
3. Sustainability
4. Affordability
5. Conservation
6. Economic Development ( combines economic development, growth and job retention)

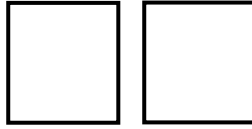
The remaining principles relating to: being defensible, being consistent, respecting history and being simple to understand and maintain are either implicit (e.g. defensible) or could not be achieved until the full rate structure review is completed (e.g. full consistency between water and sanitary rates). Further simplification of the rate structure will be undertaken in the next phase of the full review.

Rate Model Analysis

The table below compares the existing rate structures to the proposed rate structures for Phase 1 implementation of the new fixed rate charge.

	Existing Rate Structure	Proposed Rate Structure
Water	Total Charge = Volumetric charge + meter charge (\$5 minimum)	Total Charge = Volumetric charge + fixed charge (no minimum)
Sanitary	Total Charge = Volumetric charge (no fixed & no minimum)	Total Charge = Volumetric charge + fixed charge (no minimum)
Storm	Fixed Charge OR Area Charge	No Change

Whenever a rate structure change of any nature is made, some rebalancing of cost to customers occurs. Some customers will benefit and some will be required to pay more. Assuming the changes are being made to improve equity and fairness across all customers,



those who are required to pay more under the new structure have likely been receiving an unfair benefit for many years at the expense of the other rate payers. Without modifying certain parameters within the rate structure, generally lower volume users would be disadvantaged and higher volume users would see benefits. Considerable effort was undertaken to attempt to mitigate large swings from what customers pay now to what they would pay when a larger fixed charge is introduced. These mitigation measures were developed to provide a rationale position and be consistent with the principles and objectives on which the rate structure is premised going forward.

To mitigate some of the potential impacts a variety of subtle changes are suggested to the existing rate structures:

1. The water minimum charge of \$5 be eliminated
2. The first 5 cubic metres of water and sanitary use be provided at no charge for residential customers
3. The majority of the volumetric rate charges be less than the existing rates
4. Conservation premiums for second and third block rates for residential water consumption be increased to ensure that conservation is still foremost in customer's minds, given that higher fixed charges tend to dampen the financial incentive to conserve
5. The relative amounts of revenue collected between residential and non-residential be adjusted to be closer to ratios developed during the previous rate structure review
6. The first and second industrial rates be blended with the first and second institutional sanitary rates, resulting in 5 rate categories instead of 7 (see BMA report for details)
7. The fixed charge be based on the water meter size with relative cost differences based on the suggested AWWA meter equivalency ratios.

#### Impact on Low Volume Residential Water Users

The majority of residential water customers use between 10 and 15 cubic metres of water per month, as demonstrated by the bar graph in the BMA report. Only 7% of customers are in the 0 to 5 cubic metre range and 20% are in the 5 to 10 cubic metre range. The two low volume user ranges will experience an increase in their water bill, whereas the remaining 72% will see a decline if their consumption remains the same. To put this into perspective residential expenditures across Ontario were compared (table on page 12 of BMA report). London households averaging 7 cubic metres month currently pay 31% less than the Ontario average of the comparator group, while those households that average 10 cubic metres per month pay 16% less. By increasing the fixed charge, these two households would still be 21% and 14% below the comparator average cost.

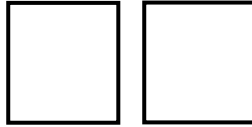
When issues of affordability are raised, those customers who are most challenged to absorb rate increases are in fixed income and/or low wage households. Many of these households are classified as commercial rental properties, in addition to single family or multi-family residential properties. It was therefore important to attempt to reduce the impact on these customer groups.

#### **Next Steps**

It is desirable to implement the fixed rate charge separately from the annual budget discussion in November and the upcoming full review of the rate structure which is intended to improve consistency (and therefore simplicity) between the water and wastewater rate structures, as well as to improve fairness and equity for the storm drainage charges.

To complete the implementation, it will be necessary to prepare a revised by-law and hold a public meeting before Council. London Hydro requires approximately three months to make the modifications to the billing system to incorporate these revisions.

The internal audit undertaken by Pricewaterhouse Coopers recommended that a fire protection charge and a construction water charge be considered to more effectively recover the cost of providing this benefit to our customers. Staff suggests that these improvements be included in the full rate structure review for phase 2 implementation. The full rate structure review would be brought back in late 2012 for Council review with implementation tentatively scheduled for mid year 2013. This timing would provide an



additional year to gauge impact of whether the economic conditions are improving for businesses, thereby allowing them to accommodate a slight increase to ensure an equitable cost sharing between residential and ICI customers.

**Conclusion**

The main cost drivers of the fixed charges relate to infrastructure renewal, and thereby we are investing in the sustainability safety and reliability of the utilities to promote economic development and support quality of life in the City. Introduction of the proposed fixed rate charges for water and sanitary will improve revenue stability, achieve sustainability of the utilities more quickly - consistent with the City's Strategic Plan; and improve fairness and equity from a user pay perspective. By changing the conservation rate premiums, the financial incentive to conserve will be maintained. Economic development will be further promoted by ensuring critical infrastructure is renewed in a timely manner and large volume users will actually pay slightly less than they are currently paying. Affordability is also maintained by adjusting meter charges and offering residential customers (individually metered) the first 5 cubic metres at no charge.

**Acknowledgements**

This report was prepared by Roland Welker, Division Manager of Water Engineering with input from Matt Feldberg, Water Demand Manager and Jason Senese, Manager Administrative Services.

<b>PREPARED BY:</b>	<b>RECOMMENDED BY:</b>
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March 27, 2012

Attachment: Appendix A - BMA Water and Wastewater Fixed Rate Review, March 2012

- Cc: S. Glickman, London Economic Development  
 M. Henderson, Corporate Management  
 M. Hayward, City Treasurer & CFO  
 J. Fleming, Planning  
 G. Macartney, London Chamber of Commerce  
 Jason Senese, Manager of Administrative Services, Finance/PEES Support