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TO:	CHAIR AND MEMBERS CIVIC WORKS COMMITTEE MEETING ON MAY 14, 2012
FROM:	TIM DOBBIE INTERIM CITY MANAGER
SUBJECT:	SHARED SERVICES UTILITY MODEL REVIEW – MAY 2012 STATUS UPDATE

RECOMMENDATION

That on the recommendation of the Interim City Manager, the following actions be taken:

- (a) This report on the status and conceptual development of the Shared Services Utility Model (SSUM) **BE RECEIVED** for information;
- (b) The methodology and Interim Steps outlined in this report **BE ENDORSED** and staff **BE DIRECTED** to proceed with the next phase;
- (c) Civic Administration **BE DIRECTED** to report back upon completion of each phase, and seek Council approval prior to proceeding to the subsequent phase along with funding sources as needed.

PREVIOUS REPORTS PERTINENT TO THIS MATTER
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June 21, 2011, Committee of the Whole, "Preliminary Report – Shared Services Model for Utilities"

September 20, 2011 Committee of the Whole, "Extending the London Hydro Model to the City of London's Water/Wastewater Utility and Other Services" (no report, presentation only)

January 9, 2012, Strategic Priorities and Policy Committee, "Community Engagement Task Force – Final Report"

BACKGROUND

During September and October 2011, Council received a number of reports and presentations regarding potential efficiencies and effectiveness that could be achieved through restructuring opportunities involving London Hydro and various utility operations currently functioning as City departments. At that time the City also received, but took no action on, a presentation and a proposal to enter into a 'Cooperation Agreement with EPCOR Utilities Inc. of Edmonton, Alberta.

Council directed London Hydro and Civic Administration to prepare a business plan that addressed a number of interests and aspects. This report is intended to provide an update on the coordinated efforts of the senior management from London Hydro and Civic Administration and seeks clarification on expectations related to some of the elements as requested by Council.

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The development and review of a Shared Services Model is anticipated to be undertaken in three phases with further Council direction requested prior to proceeding to the next phase. Each phase is comprised of several steps noted as follows:

1. Phase I - Review of a Shared Services Utility Model
2. Phase II - Establishing the Framework for Review of a Shared Services Utility Model
3. Phase III - Review, Evaluation & Approval Process of a Shared Services Utility Model

DISCUSSION

Phase I – Review of a Shared Services Utility Model

The management teams have coordinated two pieces of preliminary work, one of which has been completed and the second of which is underway. After some review, it was decided that it would be beneficial to look at the existing financial information of each organization in a consistent format. London Hydro's annual financial reporting is transitioning to International Financial Reporting Standards (IFRS) and has a number of practices and procedures that are different from the City's. The water and wastewater utilities utilize traditional municipal financial accounting (Public Sector Accounting Board), the water and wastewater utilities are budgeted and accounted for separately.

In order to establish an initial estimate of 'what might be possible (from a financial perspective)', the City and London Hydro collaborated and retained KPMG to prepare a high-level Pro Forma projection and analysis, including projected Balance Sheets, P&L Statements and Cash Flow Statements. KPMG provides financial audit services for both London Hydro and the City. The initial evaluation has indicated that there may be some fiscal opportunities. However when evaluated under a financial process similar to the one utilized by London Hydro, these opportunities may be dependent on/or modified should certain guiding principles be established. For example, London Hydro operates with a very close focus on debt-to-equity, whereas municipal utilities have taken a pay-as-you-go approach which is more of a cash based methodology. The overall review is clearly multi-faceted and it has been agreed by both senior administrations that further high level review is needed to focus on the operational impacts or synergies of any amalgamation, specifically trying to quantify the magnitude of any savings or costs related to restructuring needs. It is expected that this review will involve comparing the proposal with industry 'best practices' as documented by established benchmarking work. In Canada, the engineering firm AECOM is an industry leader with respect benchmarking and has been retained to provide this review.

These two pieces of work will provide preliminary background information and form the initial phase of work that will be essential to initiate further dialogue. The preparation of this background work has been influential in developing a process/sequence to advance this assignment, given the areas of interest indicated by Council.

Phase II – Establishing The Framework for Review of a Shared Services Utility Model

During the course of this assignment, it has become clear that London Hydro's position and approach to joint ventures, partnerships, and strategic alliances are well advanced and to some degree defined in the London Hydro Shareholder Declaration. Many of the issues raised by Council, that now form part of the resolution direction, point out that consideration should be given to development of the necessary business case, and as a first step 'guiding principles' should be established. There are also existing guiding principles that should be considered (or may ultimately require adjustment). Those documents include: the water (and sewer) financial plans, corporate financial plan, corporate strategic plan, our labour relations strategic plan, etc. Establishment of guiding principles will require significant public consultation/involvement and ratification by Council.

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Given Council's direction of October 3 and the discussion of Council on October 24, City staff have considered the potential steps needed to advance this initiative and prepare a draft Shared Services Utility Model that addresses the following points of interest identified by Council's resolution (order modified to allow for a more sequential flow):

1. Guiding principles
2. The public interest
3. Relationship with constituents
4. Public engagement
5. All regulatory and process issues
6. Labour and employment issues
7. Cost implications including the proposed salaries of reporting heads
8. Governance structure

The City will be well served to develop a clear process addressing Council direction noted above as well as meeting the "Duties of Municipality" with respect to consultation as outlined in O. Reg. 599/06 – Municipal Services Corporation. Any subsequent structural change will require that the City meet the obligations of this Regulation. A defined process will enable any unforeseen circumstances arising in the context of this process to be dealt with.

The following outlines the possible 'Interim Steps':

1. *Establishment of initial 'draft for discussion' Guiding Principles*
2. *Public review & public input on those principles*
3. *Council confirmation of guiding principles and willingness to proceed*

At the end of this phase, Council will have the opportunity to approve the 'guiding principles' meeting the cornerstone objective of the October 3, 2011 direction. Civic Administration will then be in a position to undertake the more detailed review. It is estimated that steps 1-3 will cost \$200,000 and will take 6 months to complete.

Phase III – Review, Evaluation & Approval Process of a Shared Services Utility Model

Working from guiding principles that have been established in an open and transparent fashion, we will establish a framework on which to deal with issues that may arise as noted in the preliminary EPCOR discussion--funding and sustainability strategies, provision of services beyond, the City of London approach to labour relations issues, to name a few. The following list of steps should be considered as draft, but note that the process would include going back to the public prior to finalization and recommendations to Council.

4. *Review & Evaluate existing businesses for utility/holding company model*
 - Review regulatory regime of each business (Water and Sewer), as well as corporate issues (Municipal Act, Municipal Services Corporation Regulation 599, corporate governance, etc)
 - Comment on compatibility
 - Flag areas of concern
 - Review labour relations & employment issues of each business
 - Issues arising from possible change in structure, transfer, etc
 - Other collective agreement obligations
 - Financial evaluation of existing businesses
 - Book value of assets & depreciation
 - Existing financial plans – operating and capital
 - Comment on sufficiency of existing plan
 - Potential efficiency & operational gains

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- Review operations
- State assumptions
- Indicate opportunities

5. *Bring it together, proposed governance structure & check fit with principles*

6. *Project fiscal performance*

- Consider short-term and long-term impacts on rates
- Other fiscal options (corporatizing assets?)

Long-term fiscal outlook

7. *Public review and public input*

8. *Based on evaluation of above factors and public input, staff will develop recommendations for Council to consider*

- (For discussion purposes, it is estimated that steps 4-8 will cost \$500,000 and will take 9-12 months to complete)

On the issue of ‘engagement’, there are significant considerations that must be addressed. First and foremost is the dialogue with existing staff and bargaining agents. Civic Administration have already met with and received correspondence from CUPE representatives. Engagement and dialogue must continue. Senior staff at London Hydro have also kept their employees advised and involved in the review of this concept.

Beyond the internal engagement, public interest in this matter is expected to be high based on the response back in October when the EPCOR proposal was under active consideration. The water and wastewater utilities are paid for by the users and considering the recently endorsed Community Engagement Policy, it will be important to consult broadly.

CONCLUSION

The purpose of this report is to provide an information update on progress made over the last few months. It has also become clear that more definition/direction is required for staff to advance a review that meets Council’s needs. Recommendations two and three suggest a series of ‘next steps’ that will see that direction evolve while at the same time ensuring the engagement of not only the public but also our employees.

Council has indicated an interest and identified some key parameters that should be considered in developing a draft Shared Service Utility Model. This report outlines the proposed interim steps and ballpark cost/timelines required to advance this review. Council are being asked to approve those steps, and staff will report back prior to proceeding with the balance of the work. Funding for the current conceptual review was identified earlier; subsequent funding sources will be identified as needed in follow-up reports.

PREPARED BY:	RECOMMENDED BY:
JOHN BRAAM, P.ENG. ACTING EXECUTIVE DIRECTOR, PLANNING, ENVIRONMENTAL AND ENGINEERING SERVICES & CITY ENGINEER	TIM DOBBIE INTERIM CITY MANAGER

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