

--	--

TO:	CHAIR AND MEMBERS CIVIC WORKS COMMITTEE MEETING ON JULY 17, 2012
FROM:	JOHN BRAAM, P. Eng. ACTING EXECUTIVE DIRECTOR, PLANNING, ENVIRONMENTAL & ENGINEERING SERVICES & CITY ENGINEER
SUBJECT:	RATE STRUCTURE REVIEW – FOR WATER, SANITARY AND STORM DRAINAGE CHARGES

RECOMMENDATION

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**:

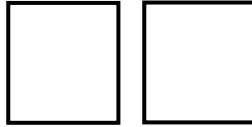
- a) The following report **BE RECEIVED** for information;
- b) the goal, objectives and principles used to develop the rate structures **BE ENDORSED** by Council, as follows:
 - Goal:** To introduce and implement a “value based” funding model for water and wastewater services
 - Objectives:** To ensure financial stability, to promote conservation and to encourage and support economic development and jobs retention
 - Operating Principles:** Fairness and equity, Sustainability and Affordability
- c) Civic Administration **BE DIRECTED** to undertake further consultation on the development of the rate structure with our stakeholders including the public, businesses and the economic development community.

PREVIOUS REPORTS PERTINENT TO THIS MATTER
--

The reports noted below can be found at:

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

- [Fixed Rate for Water and Sanitary Charges, April 2, 2012, Civic Works Committee, Agenda Item # 32](#)
- [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 15th Meeting, July 27, 2009 – Item 285, 14th 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 – 2nd Report of the Environment and Transportation Committee, Item #19 and Agenda Item #17;
- Council Proceedings 15th Meeting, July 21, 2008 – Item 241, 22nd Report of the Board of



Control, Clause #26, as amended;

- Water, Sanitary and Storm Rate Structure Review – Revisions to Current Structure, July 16, 2008 – 22nd 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 – 17th 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 – 31st 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.

BACKGROUND

Purpose

This report provides Committee and Council with an understanding of how the rate structure review will be undertaken over the next several months. The report will describe the process to be followed; the objectives, goals and underlying principles; and the input opportunities for Council and stakeholders.

Background

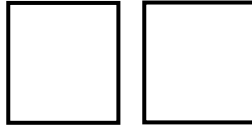
The water and wastewater systems are customer owned and supported utilities. Water and sewer rate charges provide the revenue streams needed to sustain these utilities. City staff undertake the stewardship roles to ensure the utilities are well managed and maintained for current and future generations. 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 ([July 2010 report](#)) 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.

In 2011, the priorities of the water and wastewater utilities switched to establishing a higher fixed rate portion in the rate structure to improve revenue stability. In April 2012, Council requested that the full rate structure review be completed to determine longer term impacts on the customer and the sustainability of the utilities.

Excerpt from Council Resolution of April 10, 2012

32. [Fixed Rate for Water and Sanitary Charges](#)



That in accordance with Section 17.6 of the Council Procedure By-law, the attached Staff report related to a fixed rate for water and sanitary charges BE REFERRED to the Municipal Council for its disposition; it being noted that the Civic Works Committee (CWC) was unable to reach a majority decision with respect to this matter. (2012-W10-00/F17-00)

Motion made by Councillor P. Van Meerbergen and seconded by Councillor B. Polhill to Refer clause 32 back to Civic Administration for a report back at a future meeting of the Civic Works Committee with a proposed comprehensive model which would include all phases of implementation of a new rate structure for water and wastewater.

Motion Passed

Discussion

Administration has held several internal meetings to suggest a new approach for the rate structure review which would address Committee and Council’s concerns. This report will describe an iterative approach to solicit input from both elected officials and customers in an effort to move this review forward.

The three step approach is to:

- Re-focus the goal, objectives and principles for this review that is consistent with the City’s Strategic Plan
- Develop a communications plan that circulates the information widely to all stakeholder groups and provides opportunity for input of both elected officials and customers
- Assess the impact of changes to the rate structure on budget and financial plans for both utilities

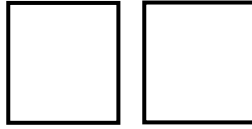
The goal, objectives and principles are shown below and are further defined in Appendix “A”. They have been abbreviated from the original 10 presented in past reports to focus on the most important issues and assist in the development of the new funding model.

GOAL	To introduce and implement a “value based” funding model for water and wastewater services
OBJECTIVES	<ul style="list-style-type: none"> • To ensure financial stability • To promote conservation • To encourage and support economic development and jobs retention
OPERATING PRINCIPLES	<ul style="list-style-type: none"> • Fairness and equity • Sustainability • Affordability

Introducing and implementing a new funding model for water and wastewater services will require a new understanding of the value of water; it is not about cost, it is not about price, it is about value – health and safety, quality of life, economic development and fire protection.

A Strategic Communications Plan will be rolled out over the coming weeks with the goal: ***To engage the citizens of London in a dialogue on the value of water.***

The communications plan will identify the strategy and tactics, key messages and delivery mechanisms required to reach and engage all audiences: the single mother receiving social assistance and raising four kids in a rented apartment; the retired couple spending six months in



sunny Florida (Snowbirds); the homeowner with a pool and a hot tub; London's business community; our world class healthcare organizations, universities and colleges; our large industries such as those in the business of producing food and beverages and the future businesses that will choose to set-up shop in London.

A properly designed funding model will balance the objectives and principles across all customer groups within the City and ensure that everyone pays their fair share for these life giving services. There remain numerous fairness and equity issues as described in Appendix "B" which need to be addressed. Invariably, modifications to the existing rate structures will see those who have been currently receiving a benefit at the expense of another customer group feeling disadvantaged. These customers will voice their concerns most loudly, while those customers who will see a lowering of what they currently pay, do not tend to voice their opinion. It is difficult for our elected officials to assess the appropriateness of the proposed changes when there is not a more balanced response.

As part of the new rate review, impact analysis of the proposed "value based" funding model will be undertaken as it relates to:

- our customers,
- the 20 year financial sustainability plans for the utilities, and
- budget impacts.

Future reporting will indicate the extent of these impacts on sample customers. Individual customer impacts can be assessed by our staff on a one-on-one basis to avoid concerns with confidentiality of business operations. Stakeholder meetings can be organized as deemed appropriate.

Next Steps

Over the next few months, progress reports will be brought forward to provide additional opportunities for input, prior to finalization of the report. A draft structure will be brought forward for full discussion with Committee to attempt to address political issues as they relate to subsidization of businesses, those who conserve or the economically disadvantaged.

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 requested by Council.

It is desirable to implement the new funding model separately from the annual budget discussion in October/November, while at the same time providing an indication of what changes may result to the budget for the proposed "value based" funding model.

To complete the implementation, following stakeholder consultation, 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 full rate structure review would be brought back in late 2012 for Council review with potential implementation by London Hydro tentatively scheduled for mid year 2013.

Conclusion

Council endorsement of the goal, objectives and operating principles will provide the basis for the development of the new "value based" funding model. The objectives and operating principles are strongly aligned with the City's strategic plan and will support economic development, health and safety, quality of life, and fire protection. A well developed communications plan will assist our customers and elected officials in understanding the value of the services provided by the utilities and assist them with decision making imperative to arriving at a balanced funding model for the current and future generation of cutomers.

--	--

Acknowledgements

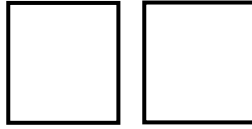
This report was prepared by Roland Welker, Division Manager of Water Engineering with input from Matt Feldberg, Water Demand Manager and Jason Senese, Manager Administrative Services.

PREPARED BY:	RECOMMENDED BY:
ROLAND WELKER, P. ENG. DIVISION MANAGER WATER ENGINEERING	JOHN BRAAM, P.ENG. ACTING EXECUTIVE DIRECTOR, PLANNING, ENVIRONMENTAL & ENGINEERING SERVICES & CITY ENGINEER

July 18, 2012

Attachments: Appendix A - **Objectives and Operating Principles**
Appendix B – **Specific Concerns with the Current Rate Structure**

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



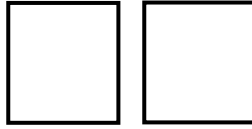
**APPENDIX A
OBJECTIVES AND OPERATING PRINCIPLES**

OBJECTIVES	DESCRIPTION
Ensure Financial Stability	In the past seven of eight years the water system has operated in a deficit position. A predictable source of income (revenue) is required to avoid a deficit when meeting operating and capital obligations. Current fixed costs for water and wastewater range from 60%-80% of the total budget expenses while the current fixed charge recovers only 1% of total costs. A new funding model will reallocate how costs should be recovered from the fixed and volumetric fees and rates.
Promote Conservation	Continued support and promotion of water conservation efforts will benefit the wise consumer (increasing premiums charged to high volume residential customers), the operating system (may reduce operating costs and capital investment needs over time), and the natural environment (reduction of energy use, of residual wastes and chemicals).
Encourage and Support Economic Development and Jobs Retention	London’s institutional, commercial and industrial (ICI) customers currently pay less for water and wastewater services than most other municipalities in Ontario. ^a The new funding model will be aligned with other economic development initiatives ensuring competitive positioning of London as place to do business thereby retaining current and attracting new businesses.

OPERATING PRINCIPLES	DESCRIPTION
Fairness and Equity	A new funding model - a reallocation of fixed and volumetric fees and rates - will ensure that all customers are charged a fair price for the water they use and the infrastructure required to deliver the service. The current rate structure or funding model that delivers a 1% recovery rate of fixed costs, which make up 60%-80% of all operating costs, means that high volume customers are paying more than their fair share for water and wastewater services. ^b
Sustainability	A new funding model will ensure availability of funding for future capital investments for infrastructure maintenance and expansion. Life-cycle planning made possible with assured infrastructure financing will prove to be more efficient and cost effective and minimize social disruption associated with infrastructure failures.
Affordability	A new funding model (fixed and volumetric fees and rates) will offer affordable fees and rates for all customers while ensuring that the full cost of service is being recovered. Over the long term, customers will pay less as a result of sustainable infrastructure renewal and conservation efforts.

^a Water and Wastewater Cost Recovery Review, BMA Management Consulting Inc., March 24, 2012

^b Water and Wastewater Cost Recovery Review, BMA Management Consulting Inc., March 24, 2012



APPENDIX B

Specific Concerns with the Current Rate Structure

(excerpt from May 7, 2008 BOC Report, Agenda Item #7, page 36 – text edited in 2010 is in Italics)

Over the course of various meetings and discussions with customers in the last few years, many issues concerning the current rate structure. It is recognized that some of these issues may be purely technical, while others are more of a political nature, e.g. should rates be used as an economic development incentive or as a low income subsidy to promote better sanitation in poorer households. Appendix “B” of the May 7, 2008 BOC Report *provided* a summary of the issues and provided commentary and recommendations by Administration to set the context and assist in the decision making process.

While it is important to review our practices from time to time to ensure we are following the best practices and this is one of the key drivers for suggesting that current rate structures be changed, there are several examples of improvement opportunities which staff feel need to be addressed to make the rate structures more fair and equitable, *and achieve the principles which were established at the start of the rate review process* including:

- Increase difference between water block rates to further promote water efficiency in the residential sector
- *Fire protection costs are currently recovered based on the amount of water consumed, which is not reflective of actual costs, particularly in the ICI sector*
- Multi-family bulk metered properties currently are not subject to a conservation rate which can result in water wastage since the cost is distributed equally among all the residents – *the threshold for higher block rate charges for these buildings would be based on the single family residential threshold times the number of units in the building or development*
- Achieve a greater degree of consistency between water, sanitary and storm rates in terms of the rate structure and rationale for customer differentiation
- Demonstrate why there is a difference between residential and ICI
- Run the utilities more like a business, charging for what it costs to deliver the service versus pricing the service based on what the customer does, *thereby establishing a defensible cost basis versus what may appear to be a market pricing approach or worse favouritism of one customer over another*
- Water is charged on the basis of a metered account and meter volumes are not aggregated for ICI customers, while sanitary classifies customers based on the sum of all the customer’s *metered accounts* over the year, requiring annual updating to ensure customers are in the correct classification *based of thresholds of annual consumption*
- *Flat Rate* Charges for storm drainage service is based on the number of water meters a property has instead of the area of the property (currently only approximately 100 industries are charged based on area), examples:
 - a 130 unit townhouse development pays almost the same storm charge as a single family residential property
 - a commercial plaza or hospital campus of 30 ha may pay less than 6 single family homes equating to 0.6 ha , i.e. pay less for 50 times the area
- *Storm drainage servicing costs bear no relationship to water consumption, yet the current storm area charge offers a lower area rate to large water consumers*
- Some buildings with 5 or more units are classified as high rise and receive the commercial sanitary rate, whereas some buildings of 5 or more units are classified as multi-family and pay the residential sanitary rate – *buildings of up to 19 units are more reflective of residential pipe value costs and should be deemed as residential customers, whereas buildings of 20 units and 4 stories or more are defined as “high rise” and are more characteristic of larger commercial buildings with respect to pipe value and should therefore be classified as an ICI customer*
- Some customers pay storm drainage charges even though they do not see an obvious benefit.
- Some property owners do not pay any storm charge because they do not have a water meter, examples, lands under development and vacant parcels. If storm charges were part of the tax base, then these property owners would pay for storm servicing based on their assessment. *In subsequent discussions with these customer types, it was determined that achieving equity would disadvantage these customers, adding considerable cost to properties which are potentially developing which do not have a revenue source to support the new costs. This type of a charge will be reviewed in future updates.*