DRAINAGE INDICATIVE RATE – REVISED FOR 2017 AND 2018

EXECUTIVE SUMMARY

Administration has analyzed options and is recommending an opportunity to reduce the approved drainage charge increases for 2017 and 2018. Through the process leading up to the presentation of the Action Plan budget and business plan, Administration received Council approval for increases to the drainage monthly charge that funds the Drainage line of service. The approved increases reflected a 19.1 per cent increase in the monthly charge each year, which translates into annual increases in the range of $1.76 to $2.97 per month over the 2015-2018 business plan. These increases were approved by Council in support of advancing the performance of the drainage portfolio and achieving compliance with the Drainage Financial Plan.

In response to the financial impacts felt by the Calgary community related to the current economic conditions, Administration has undertaken a review of all opportunities to reduce the magnitude of annual increases for 2017 and 2018. As a result of this review, Administration is recommending that the Action Plan approved 2017 and 2018 drainage charge increases be revised to reflect a 7.4 per cent per year increase in 2017 and 2018 (monthly charge increases of $0.97 in 2017 and $1.03 in 2018).

This proposed scenario leverages efficiencies, while maintaining capital investment required to build, upgrade, and maintain infrastructure to provide high quality services to customers. Compliance with financial policies is maintained with the exception of the requirement to build the 10 per cent of revenues sustainment reserve balance by 2018, which will be delayed until 2022. In comparison to a zero per cent increase scenario, a 7.4 per cent per year increase offsets some risk of off-site levy revenue not materializing due to the uncertainty of growth and development, and will have less impact on the drainage charge increases for the 2019-2022 timeframe.

ADMINISTRATION RECOMMENDATIONS:

That Council direct Administration to:

1. Present an operating budget adjustment for 2017 and 2018 and related bylaw amendments based on the reduced drainage charge increases in Attachment 2 as part of Mid Cycle Adjustments; and
2. Report back in Q1 2017 with revisions to the Drainage Financial Plan that integrate industry best practice and the change to the timeframe of building the sustainment reserve balance.

PREVIOUS COUNCIL DIRECTION / POLICY

On 2013 April 22, Council adopted Drainage Financial Policies (UCS2013-0044), which included financial policies specific to the Drainage line of service.

On 2014 March 17 Council received Drainage Financial Plan 2015-2018 for information (UCS2014-0022) which included recommended financial targets and levels of service.

On 2014 May 05 Council approved C2014-0324, 2015-2018 Indicative Drainage Charge, directing Administration to develop 2015-2018 Action Plan based on an indicative drainage charge that reflected a desired service level in five program areas in the Drainage line of service. The resultant charge increase was 19.1 per cent per year.

BACKGROUND
The Water Services and Water Resources business units manage and operate the Drainage line of service as a self funded activity. In this model, the drainage charge is set to recover the full costs of providing the drainage services. In addition to operating within relevant Council and Administrative policies, Drainage does maintain financial policies specific to its operations. These policies, their associated targets and an established timeline for compliance, comprise the Drainage Financial Plan.

On 2014 May 05 Council approved report C2014-0324, 2015-2018 Indicative Drainage Charge, directing Administration to develop 2015-2018 Action Plan based on an indicative drainage charge that reflected a desired service level in five program areas in the Drainage line of service. The resultant charge increase was 19.1 per cent per year, and this enables advancement in the program areas:

- Regulatory and environmental protection;
- Maintaining assets;
- Community drainage improvements;
- Flood recovery and resiliency; and
- Financial plan compliance.

Table 1 below shows the increases to the monthly Drainage charge that were approved as part of Action Plan.

Table 1. Action Plan Approved Monthly Drainage Charge Increases

	2015	2016	2017	2018
Incremental Increase	$1.76	$2.09	$2.49	$2.97
Monthly Drainage Charge	$10.96	$13.05	$15.54	$18.51

INVESTIGATION: ALTERNATIVES AND ANALYSIS
In response to the current economic conditions, Administration has undertaken a review of all opportunities to reduce the magnitude of drainage charge increases for 2017 and 2018. The self supported and capital intensive nature of the drainage business is a driver of the drainage charges, in addition to the requirement to comply with the Drainage Financial Plan.

These drivers, and the financial performance of Drainage relative to its plan to date, do present an opportunity to reduce the magnitude of the increase in the short term. However, reducing charge increases in the short term will have an impact on drainage charges in the next business cycle.

Based on ability to vary factors and drivers in drainage charges, Administration presents the following two options for reducing the currently approved increases:

- Zero% Increase: Reduces the currently approved 19.1 per cent per year increase in 2017 and 2018 to zero per cent in 2017 and 2018, with a higher increase forecast for 2019-2022; and
- 7.4% Increase: Reduces the currently approved 19.1 per cent per year increase in 2017 and 2018 to 7.4 per cent in 2017 and 2018, with a similar increase forecast for 2019-2022.

Scenarios are shown in Figure 1 and summarized in Table 2 below. With the exception of building the sustainment reserve balance by 2018, compliance with current financial policies is maintained under both scenarios. The key difference between these scenarios is their impact to the charge increases predicted for the 2019-2022 timeframe.

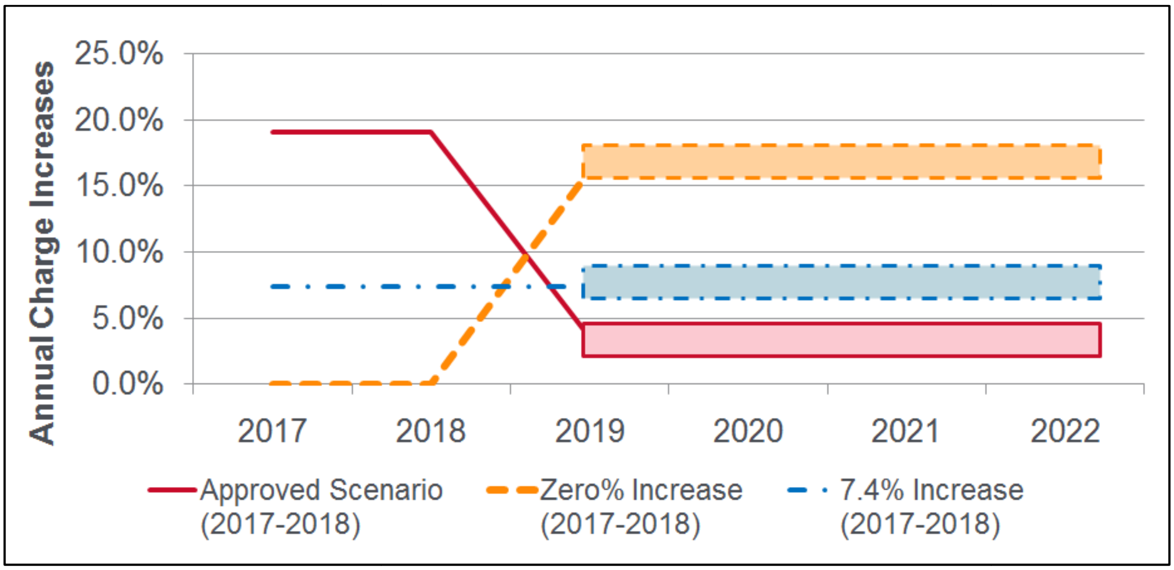

Figure 1. Scenarios for Charge Increases in 2017 and 2018, and Impact on Future Charges

Table 2. Impact of Scenarios on Drainage Financial Policies

2017 and 2018 increases	Operating Budget	Capital Priorities	Cash for Capital Maint.	Maximum Debt $B (Year)	Max Debt Service % (Year)	10% of Revenue Reserve Balance	Indicative Annual Increase (2019-22)
Zero %	99% of Action Plan	100%	100%	$0.285 (2022)	29.5% (2019)	2022	16 to 17%
7.4% (+$0.97 in 2017) (+$1.03 in 2018)	99% of Action Plan	100%	100%	$0.293 (2022)	27.3% (2021)	2022	7 to 8%

To mitigate the impact of the reduced increases in these scenarios, Administration identified efficiencies that can be achieved to reduce operating expenditures by 1 per cent. No service reductions are recommended, in order to maintain the service levels in Council's priority program areas of regulatory and environmental protection and maintaining assets programs. Maintaining services ensures the same level of priority is placed on these program areas as was indicated in the Action Plan approved drainage charges.

No capital related mitigations are recommended on the basis that the capital priorities identified in Action Plan are still required, and that investment according to the recast budget will provide stimulus in this economic downturn.

Also key to mitigating the charge reductions, is leveraging the funds in the drainage sustainment reserve, and delaying achieving the 10 per cent of revenues sustainment reserve balance from 2018 to 2022.

Administration is recommending that the Action Plan approved 2017 and 2018 drainage charge increases of 19.1 per cent be revised to reflect a 7.4 per cent increase in 2017 and 2018. This scenario leverages efficiencies while maintaining capital investment required to build, upgrade, and maintain infrastructure to provide high quality services to customers. It maintains service levels in the program areas of regulatory and environmental protection, maintaining assets, community drainage improvements and flood recovery and resiliency, by adjusting the timeframe for financial plan compliance. In comparison to a zero per cent increase scenario, a 7.4 per cent per year increase offsets some risk of off-site levy revenue not materializing due to the uncertainty of growth and development, and will have less impact on the drainage charge increases for the 2019-2022 timeframe. The current year-end projection for off-site levy revenue in drainage is $3.9 million unfavourable to budget.

The recommended scenario offers the monthly and annual savings in Table 3 to all Drainage customers, relative to the Action Plan approved increases.

Table 3. Customer Savings - 7.4% Charge Increases in 2017 and 2018 Scenario

	2017	2018
Annual customer savings relative to Action Plan approved charges	$18	$42

Stakeholder Engagement, Research and Communication

The Water Utility, in partnership with Finance, manages expenditures within the operating and capital budgets approved by Council, forecasts the future requirements to deliver services to Calgarians, and reviews progress on compliance with the financial plan. This work is overseen by a steering committee of operational, financial and strategic staff. Financial benchmarking is also performed annually to compare the costs associated with utility and drainage services provided in Calgary against other municipalities across Canada.

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Strategic Alignment
A focus on the financial capacity and sustainability enables UEP to deliver its commitment on three Council Priorities:

- To support a city of inspiring neighbourhoods, UEP provides the infrastructure needs of a growing city, enhances The City's ability to prepare/respond to natural disasters, builds resiliency to flooding.
- Contributing to a healthy and green city UEP leads by example to protect public health and the environment, and ensure regulatory compliance.
- The financial discipline demonstrated through Drainage's performance within its financial plan is an example of commitment to a well-run city.

Increasing the financial capacity and sustainability in the Drainage line of service aligns with The City's Long Range Financial Plan and the Municipal Development Plan. Ensuring that there is sufficient funding available to support growth, operate and maintain the systems, and expand and upgrade the plants also aligns with The City's 2020 Sustainability Direction, and the Corporate Growth Management Framework.

Social, Environmental, Economic (External)
The current economic downturn has affected the Calgary community. With reduced increases for 2017 and 2018, Drainage can still ensure that the social, environmental and economic goals are delivered under sound and sustainable financial policies, while reducing the magnitude of monthly drainage charge increases for Calgarians.

Financial Capacity
Current and Future Operating Budget:
Drainage has made considerable progress on the financial sustainability; however, continued compliance with the financial targets set out in the financial plan would require maintaining the Council approved charge increases for the 2015-2018 budget cycle.

A one per cent reduction in expenditures for operating the drainage line of service can be achieved through the efficiencies that have been identified. Combined with a delay in the building of the sustainment reserve balance from 2018 to 2022, these create the financial capacity required to absorb the impact of smaller increases in 2017 and 2018.

Overall outstanding debt required to support capital investment, and the debt service ratio, are forecast to be higher under the reduced scenario than with approved drainage charge increases. These can be accommodated within the overall debt and debt servicing limits of the corporation.

Current and Future Capital Budget:
The recommended increases for 2017 and 2018 are adequate to support the expected delivery of approximately $70M in capital projects annually over the remainder of this business cycle. The capital spend includes flood projects that are funded through a variety of mechanisms including disaster recovery programs, funding from other levels of government for drainage and flood resilience projects as well as the drainage charge.

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Per the recommendation approved by Council on 2015 November 25, in report C2015-0855, Water Resources is undertaking a recast of the capital budget for the Drainage line of service. The recast process will result in a capital budget more closely aligned with anticipated capital spend, and still ensure that the investment commitments made in Action Plan are fulfilled. Once the budget is recast, Water Resources will deliver capital through a process with additional controls to ensure that budget is allocated to highest priority projects, when they are ready to proceed and with the most accurate cost estimates available.

Risk Assessment

Achieving compliance with the financial targets set out in the financial plan will help ensure a financially sustainable future for the Drainage line of service. Considerable progress towards targets has been made, and ongoing compliance until the end of 2018 would require maintaining the approved increases from Action Plan. Delaying building the sustainment reserve balance to 2022 from 2018 extends the period of time in which the business does not have reserve funds to provide cash flow for minor fluctuations in operating and capital budget expenditures, or to mitigate the risk of period shortfalls in projected revenue.

The approved off-site levy rates increase forecasted revenues in future years, and this may decrease pressure on drainage charges in 2019-2022. However, these revenues are still uncertain due to the current economic environment.

REASONS FOR RECOMMENDATIONS:

In response to the impact the current economic downturn is having on the Calgary community, Council is requested to direct Administration to revise the Action Plan approved 2017 and 2018 drainage charge increases to reflect a 7.4 per cent per year increase in 2017 and 2018. This scenario leverages efficiencies, while maintaining capital investment required to build, upgrade and maintain infrastructure to provide high quality services to customers. It maintains service levels in the program areas of regulatory and environmental protection, maintaining assets, community drainage improvements and flood recovery and resiliency, by adjusting the timeframe for financial plan compliance. In comparison to a zero per cent increase scenario, a 7.4 per cent per year increase offsets some risk of off-site levy revenue not materializing due to the uncertainty of growth and development, and will have less impact on the drainage charge increases for the 2019-2022 timeframe.

ATTACHMENTS

1. Drainage Indicative Rate – Revised for 2017 and 2018
2. Recommended 2017 and 2018 Drainage Rate Increases
3. Presentation: Drainage Indicative Rates – Revised for 2017 and 2018