

## **DRAINAGE FINANCIAL PLAN PROGRESS REPORT**

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### **EXECUTIVE SUMMARY**

In 2013, Council approved Drainage financial policies to strengthen the operational management of Drainage and to secure its long term financial outlook. A Drainage Financial Plan that integrates financial targets with the approved Drainage financial policies has been developed. The establishment of financial targets allows Water Resources and Water Services (the Utilities) to monitor progress towards long term goals and provide the flexibility to respond to changing circumstances.

This report provides an update on the Drainage line of service (Drainage) Financial Plan, in particular, the progress towards achieving the financial targets and maintaining compliance with the financial policies set out in the Drainage Financial Plan. Additionally, this report also provides the results of a recent review of the continued relevance of Drainage's financial policies and targets in relation to the goal of financial sustainability and utility industry best practices.

Drainage is in compliance with the financial targets set out in the Drainage Financial Plan, helping to ensure a financially sustainable future based on the current levels of service. Maintaining compliance is dependent on the stormwater drainage charge increases approved in Action Plan 2015-2018.

A progress report (the Attachment) is being provided for the purpose of:

- Demonstrating Drainage's performance in accordance with the plan.
- Summarizing the impacts on the Drainage of the new off-site levy bylaw (C2016-0023, Bylaw 2M2016) approved by Council 2016 January 11.
- Updating Council on the assessment and recommendations resulting from the review of financial policies and targets that was undertaken by an external consultant.
- Reporting on the outcome of work that has been undertaken to scope the requirements and implications of implementing an impervious area billing system.
- Completing necessary steps in advance of the Cost of Service study that will be undertaken in 2017.

### **ADMINISTRATION RECOMMENDATION:**

That the SPC on Utilities and Corporate Services recommends that Council receive the Drainage Financial Plan Progress Report for information.

### **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.

Additionally, on 2014 May 05 (C2014-0324, 2015-2018 Indicative Drainage Charge) Council directed Administration to incorporate a cost of service study and a review of the Drainage

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Financial Plan, including program areas for potential acceleration in 2019-2022, into the 2015-2018 Action Plan; and to report back no later than 2016 June with an update on Drainage Financial Plan progress.

On 2014 October 06 Council approved the Drainage Cost of Service Study (UCS2014-0612) directing Administration to scope the requirements and implications of implementing an impervious area billing system and provide a progress report with the update on Drainage Financial Plan progress to the SPC on Utilities and Corporate Services no later than 2016 June.

### **BACKGROUND**

The Water Services and Water Resources business units have operated the Drainage line of service as a self funded activity since 2004. In this model, the stormwater drainage fees and charges are set to recover the full costs of providing drainage services. In addition to operating within relevant Council and Administrative policies, financial policies specific to Drainage operations are maintained. These policies, their associated targets and an established timeline for compliance, comprise the Drainage Financial Plan.

The Drainage financial policies were first established in 2013 to provide improved financial capacity and sustainability to meet the challenges of maintaining service and responding to growth. In 2014 financial targets and levels of service for Drainage were approved and a timeline for compliance by 2018 was set.

### **INVESTIGATION: ALTERNATIVES AND ANALYSIS**

#### *Revenue*

Drainage is funded by revenue based on the Council-approved stormwater drainage charge and is supported through Council approved off-site levy rates that recover costs associated with new growth. The off-site levy bylaw (C2016-0023, Bylaw 2M2016) approved by Council 2016 January 11 included levy rates that will fund the full cost of infrastructure investments for new development.

Off-site levies in Drainage have historically not been reflected as revenue in the operating budget. In conjunction with the new off-site levy bylaw, off-site levy revenue will be recognised as revenue.

A net-zero budget adjustment, that will be presented to Council in 2016 June, has been approved to recognize changes from the 2016 off-site levy bylaw as well as the revised revenue recognition approach. With off-site levy revenue being recognized in the operating budget, it might appear that revenue for the line of service has increased significantly. In reality, this is strictly an accounting change and will not impact the approved stormwater drainage charge increases for the remainder of this business cycle. Under the new off-site levy bylaw, Drainage levy rates are set to recover the cost associated with new growth, in the same way as under the former bylaw. In addition, revenues are still uncertain due to the current economic environment.

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### *Impervious Area Billings*

Water Resources has scoped the requirements and implications of implementing an impervious area billing system and determined that considerable effort is required to establish fair and defensible rates, and to ensure that Drainage's financial sustainability and water resource management goals are achieved.

There are numerous activities underway in the 2015-2018 business cycle that are providing greater clarity around the investments required to provide an appropriate Drainage level of service and ensure river health. This will support understanding the full cost of providing the Drainage line of service now, and in the future. This includes improved understanding of the costs associated with a customer's contribution to the drainage system, as well as considerations of how costs associated with municipal infrastructure are recovered.

To set a dynamic rate structure that reflects the full cost of providing drainage services, the 2017 Cost of Service Study will focus on developing a complete picture of the revenue requirement for Drainage. It is expected that, with appropriate engagement and required technology enablement, a program will take six to eight years to form a stormwater rate that complies with cost of service guiding principles.

The water resource management perspective requires that further tools and programs to encourage customers to be aware of and manage their impact on the system, while protecting the watershed, are made available. These aspects of Drainage services, including credit and incentive programs and the investments required to support them, will be reported on as part of watershed management planning updates, and will inform the Drainage Cost of Service Study for 2019-2022.

### *Capital Investment*

Water Resources manages the long term capital requirements for Drainage through their ten-year Water Infrastructure Investment Plan (WIIP). Investment is required to meet the increasing demands on the drainage system in response to regulatory and environmental protection requirements and Calgary's ongoing population growth. Optimum levels of service also require maintenance of the existing, and growing, system. There are ongoing programs to evaluate, monitor and identify infrastructure in the drainage system that are in need of repair, replacement or upgrading. These programs ensure that levels of service to customers are maintained.

The City of Calgary has a Wastewater Approval to Operate that specifies regulatory requirements under the Environmental Protection and Enhancement Act and requires renewal in 2018 through negotiations with Alberta Environment and Parks. Changes to targets, such as sediment loadings to the rivers, within the Wastewater Approval to Operate may impact the degree of investment required in Drainage to ensure continued compliance to regulations.

In addition to flood resiliency, capital investments within the WIIP are categorized using four investment drivers as shown in the table below.

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Investment Driver	Objective	Percentage of Water Infrastructure Investment Plan (WIIP)
Maintain assets	Maintaining, protecting and extending the life of infrastructure investments.	15% - 20%
Regulatory & Environmental Protection	Continuing to meet increasingly stringent regulatory and environmental protection requirements.	15% - 20%
Service	Continuing to provide reliable and high quality services to meet the needs of citizens.	25% - 30%
Growth	Providing infrastructure to meet the needs of a growing city.	35% - 40%

A driver of investment within the Service category is the Community Drainage Improvement (CDI) program that delivers stormwater infrastructure upgrades in older communities, where the historical level of service during floods or storm events does not meet current service standards. The planning and delivery of the CDI program is proceeding according to plan, and opportunities to accelerate projects in the CDI stream of work are evaluated on an ongoing basis.

### *Operating Areas*

Drainage line of service is managing within the operating budget approved in Action Plan. Monitoring and active management of Drainage operating expenditures is ongoing.

With an annual capital spending plan of \$50 million over the next 10 years, 40 percent of which supports growth, the operating costs of these investments will continue to be a significant consideration for Drainage.

Implementation of recommendations from the Zero Based Reviews (ZBR) – complete in Water Services, and underway in Water Resources, is expected to have future benefit realized in Drainage and will ultimately reduce some of these pressures on the operating budget.

### *Progress on Drainage Financial Plan*

The policies and targets within the Drainage Financial Plan are used on an ongoing basis to guide financial management decisions and measure financial performance. A summary of performance as at the end of 2015 relative to established targets is provided in the table below.

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Policy Area	Financial Plan Target	2015 Actual
Debt limit	Maximum \$300 million	\$169 million
Debt service	Maximum 40% of total revenues	31.3% of total revenues
Cash financing of capital maintenance	100%	100%
Sustainment reserve	10% of total revenues	17.5% of total revenues

Drainage is in compliance with the financial targets set out in the Drainage Financial Plan, helping to ensure a financially sustainable future based on the current levels of service. Maintaining compliance is dependent on the stormwater drainage charge increases approved in Action Plan.

### *Next steps*

Along with ongoing focus on achieving the financial policies by 2018, Drainage will concentrate on:

- Any required revisions to the Drainage financial policies and targets, reporting back in Q1 2017 ahead of the next Cost of Service study;
- A re-cast of the 2016-2018 capital budget for Drainage that ensures the investment commitments made in Action Plan are fulfilled and opportunities to deliver a higher level of service within the same planned capital spend are considered;
- Developing a complete picture of drainage revenue requirements based on defined service levels and priorities as part of the Cost of Service study that will inform 2019-2022 rates; and
- Aligning policy areas with recommendations to be implemented from Water Resources ZBR and leveraging any financial benefits from both the Water Services, and Water Resources ZBRs to advance financial position of Drainage.

### **Stakeholder Engagement, Research and Communication**

The Utilities and Finance have undertaken the work to review progress on compliance with the financial plan. This work is overseen by a steering committee of operational, financial and strategic staff, and has been completed leveraging expertise across business units, as well as independent financial consultants. Financial benchmarking data was also reviewed, which compared the Utilities against other municipalities across Canada.

### **Strategic Alignment**

A focus on the financial capacity and sustainability of the Drainage line of service enables Utilities & Environmental Protection (UEP) to deliver its commitment on three Council Priorities:

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- To support a city of inspiring neighbourhoods, Utilities provides the drainage infrastructure needs of a growing city, enhances The City's ability to prepare/respond to natural disasters, and builds resiliency to flooding.
- Contributing to a healthy and green city Utilities, and UEP, lead 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 of Drainage 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 also aligns with The City's 2020 Sustainability Direction, and the Corporate Growth Management Framework.

### **Social, Environmental, Economic (External)**

Drainage services are fundamental to the community and the larger watershed. Compliance to the Drainage Financial Plan policies and targets will ensure that the social, environmental and economic goals of the UEP are delivered under sound and sustainable financial policies.

### **Financial Capacity**

#### **Current and Future Operating Budget:**

Drainage is in compliance with the financial targets set out in the Drainage Financial Plan, helping to ensure a financially sustainable future based on the current levels of service. Maintaining compliance is dependent on the stormwater drainage charge increases approved in Action Plan 2015-2018.

Drainage line of service is managing within the operating budget approved in Action Plan. Implementation of ZBR recommendations and other efficiencies are expected to have future benefit within Drainage and will ultimately reduce some of these pressures on the operating budget.

#### **Current and Future Capital Budget:**

Stormwater drainage charge increases approved in the 2015-2018 business cycle are adequate to support the expected delivery of \$50M in capital projects annually. The capital budget approved in Action Plan was built based on the requirement to deliver this \$50M annually, and according to the split between capital investment drivers identified in the WIIP.

In addition to what is required to expand and maintain the Drainage system, there are capital investments needed to address and mitigate against flood events. Provincial and federal funding is essential for these investments. Presently, flood recovery, mitigation and resilience investments are planned among the Utilities and Drainage investment plans.

Per the recommendation approved by Council on 2015 November 25, in the Proposed Adjustments to the 2016 Budget (C2015-0855) Water Resources is undertaking a recast of the capital budget for Drainage. The recast process will result in a Drainage capital budget more closely aligned with anticipated capital spend, and still ensure that the investment commitments

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made in Action Plan are fulfilled. Once the budget is recast, Water Resources will deliver Drainage 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**

Maintaining compliance with the financial targets set out in the Drainage Financial Plan will help ensure a financially sustainable future for the Drainage line of service. Maintaining compliance is dependent on the stormwater drainage charge increases approved in Action Plan.

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

### **REASON(S) FOR RECOMMENDATION(S):**

This report provides an update on Drainage's progress within its plan for financial sustainability. The report demonstrates performance in accordance with the plan and summarizes the impacts of the new off-site levy bylaw. It also provides an update on the results of an external review of financial policies and targets and on work that has been undertaken to scope the requirements and implications of implementing an impervious area billing system.

Confirming any changes to financial policies in Q4 2016 will be an important step prior to undertaking a cost of service study for the Drainage line of service that will inform the stormwater drainage charges for 2019-2022.

### **ATTACHMENT**

Drainage Financial Plan 2015-2018 Progress Report