

The Regional Municipality of York

Committee of the Whole
Environmental Services
December 10, 2020

Joint report of the Commissioner of Environmental Services
and
Commissioner of Finance

2021 Water and Wastewater User Rates

1. Recommendations

1. Regional Council confirm the previously approved 2.9% increase in the combined water and wastewater wholesale rate for the year beginning April 1, 2021, increasing the rate from the existing \$3.07 per cubic meter to a rate of \$3.16 per cubic meter.
2. Regional Clerk circulate this report to the local municipalities.

2. Summary

In April 2020, in response to the COVID-19 pandemic, Council decided not to proceed with a planned water and wastewater rate increase for 2020, instead maintaining user rates at their 2019 level. Any operating shortfall due to changes against budget will be drawn from rate stabilization reserves. Using rate stabilization reserves to make up any 2020 shortfall would still allow for a one-year rate increase of 2.9% for 2021, which was previously approved in 2015. After the Region completes a User Rate Study in Q2 2021, Council will be asked to consider recommendations for a new multi-year plan for future rates.

Key Points:

- Rate stabilization reserves were established to cover unforeseen fluctuations in revenue and expenditures. A draw from these reserves will be used to cover any 2020 revenue shortfall
- The 2.9% rate increase proposed for 2021 strikes a balance between the shorter-term economic impacts of COVID-19 and the long-term need for the Region to achieve full cost recovery from water and wastewater rates. The proposed 2021 rate is expected to raise the annual household bill by \$18, on average, if local municipalities fully pass the increase on to households
- The 2021 User Rate Study will assess COVID-19 impacts and other pressures in more detail to recommend rates in 2022 and beyond that will ensure long-term financial sustainability for water and wastewater

3. Background

York Region and local municipalities are responsible for providing water and wastewater services under a two-tier structure

York Region and its nine local municipalities are responsible for providing and delivering drinking water and safely managing wastewater for more than one million residents. Almost all water and wastewater users depend on Regional and local municipal systems that are physically connected.

The Region sets a blended rate for water and wastewater that it charges local municipalities. Local municipalities in turn provide services directly to retail customers, and the rates they set ultimately determine customer billing. On average, over half of the revenue generated at the local level is paid to the Region.

Without direct access to Lake Ontario, more than 90% of the Region's drinking water needs are met through long-term service agreements with Peel Region and the City of Toronto. Groundwater wells and surface-water treatment plants in the Region provide the balance of water and wastewater needs.

Roughly 85% of the Region's wastewater is conveyed to Duffin Creek plant in Pickering, which the Region owns jointly with Durham Region, while 10% goes to Peel Region and the remainder is treated at Region owned facilities.

The Region has committed to full cost recovery through user rates

Although water and wastewater rates in Ontario are not formally regulated, provincial statutes and guidance underscore the importance of financial sustainability for water utilities. One of the recommendations from the Walkerton Inquiry in 2002 was that the municipal sector raise adequate revenue for their water systems locally, without reliance on other levels of government. Since then, York Region Council has prioritized the financial sustainability of its water and wastewater systems by phasing in full cost recovery pricing.

In October 2015, Regional Council approved a plan that would see user rates cover the cost of providing the Region's water and wastewater services by 2021, including long-term asset management needs. Development charges pay for most of the initial construction costs to meet the needs of growth. The plan was based on a model that forecasts annual consumption and costs and reflects the principle of fairness to users over time, also called intergenerational equity.

The plan included annual rate increases of 9.0% for each of the first five years, including 2020. In 2021, the year in which full cost recovery would be achieved, the increase would be 2.9%.

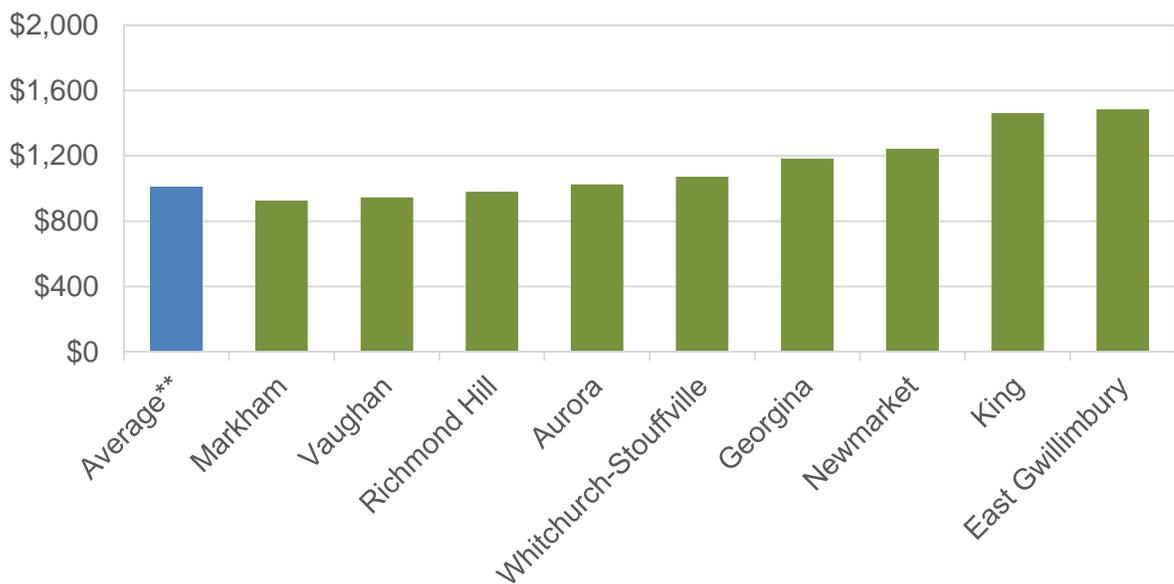
For prudence, the plan required an annual review of results against forecast, created a rate stabilization reserve to cover short-term fluctuations, and allowed rates to be adjusted if longer-term trends appeared to differ significantly from forecasts.

From 2016 to 2019, the rate model that informed the 2015 approvals was reasonably accurate in predicting underlying trends, including a general downward trend in per-capita flows of both water and wastewater. Contributions have been made to stabilization reserves in years of surplus, and a draw was made in 2017 to mitigate a revenue shortfall.

Average bills vary across the nine local municipalities but are consistent with those of Ontario comparators

The average household bill across the Region is estimated to be \$1,010, and ranges from \$925 in Markham to \$1,485 in East Gwillimbury (Figure 1). Average bills in the Region are in line with those in nearby jurisdictions, assuming residents’ consumption is similar (Figure 2). The Region’s average bill is lower than average bills in the Niagara and Waterloo regions which, like the Region, deliver water and wastewater services through a two-tier system.

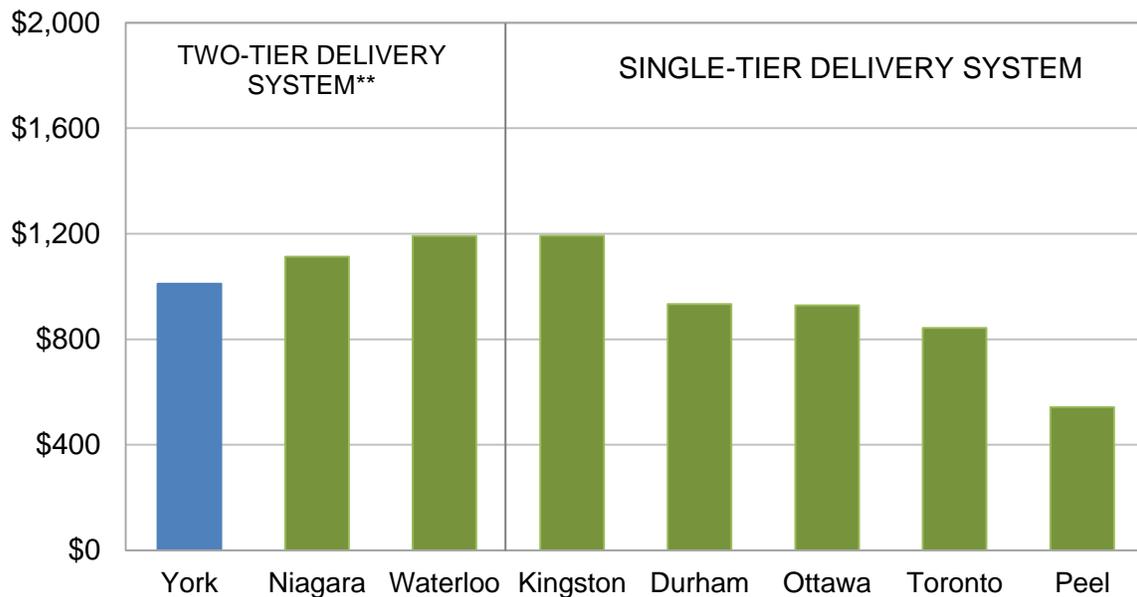
Figure 1
Average 2020 Household Bill in York Region*



* Bill based on published 2020 rates as at October 2020 and average household water consumption of 207m³ per year

** Weighted average across local municipalities by population

Figure 2
Average 2020 Household Bill in selected Ontario jurisdictions*



* Bill based on published 2020 rates as at October 2020, and average household water consumption of 207m³ per year

** Weighted average bill across lower-tier municipalities by population

COVID-19 financial concerns triggered relief measures for 2020

On March 11, 2020, the World Health Organization declared a pandemic as numerous countries reported cases of COVID-19. In line with measures taken by other jurisdictions to prevent the spread of COVID-19, Ontario closed all public schools the next day, and many workplaces were subsequently required to close or curtail their operations. By the beginning of April, more than two million Canadians, or about 10% of the labour force, had applied for employment insurance.

On April 2, 2020, a [report](#) entitled “Partnering with Local Municipalities to Support Residents and Businesses Impacted by COVID-19” was brought to Council. The report outlined the economic impact of COVID-19, described relief measures that local municipalities were considering or had already taken, and recommended measures at the Regional level. Council approved Clause 2 of the report, which kept the Region’s water and wastewater rates at their 2019 levels for 2020, foregoing the previously approved 9% increase, and required staff to report back on the financial implications. This report outlines financial impacts and recommends ways to address them.

2021 User Rate Study will inform rates starting in 2022

The 2015 rate plan assumed that a new User Rate Study would be undertaken to inform user rates after 2021. Work on this new study is underway and in Q2 2021 staff will bring multi-year options forward to Council for implementation in 2022 and beyond.

The 2015 study and related plan focused on achieving full cost recovery by the end of the six-year rate approval in 2021. Now that the Region is about to achieve that goal, the focus will shift toward maintaining full cost recovery, including monitoring future risks to the plan.

4. Analysis

Foregoing the 9% 2020 rate increase translates to a \$32.5 million revenue shortfall based on budgeted flows

User rate revenue in the Region's Budget for 2020 and 2021 was based on originally approved increases of 9.0% in 2020 and 2.9% in 2021.

Rates normally change on April 1st each year. Based on budgeted flows, the decision not to increase the rate on April 1, 2020, translates into a total shortfall in expected revenue of \$32.5 million over 12 months. For the period April 1 to December 31, 2020, the revenue shortfall was forecast to be \$25 million based solely on the rate deferral, with projected revenue for the year going from \$385 million to \$360 million. In fiscal 2021, the impact amounts to \$7.5 million for the period January 1 to March 31.

The actual year end shortfall compared to budget will be determined once actual flows and COVID-19 related impacts are known.

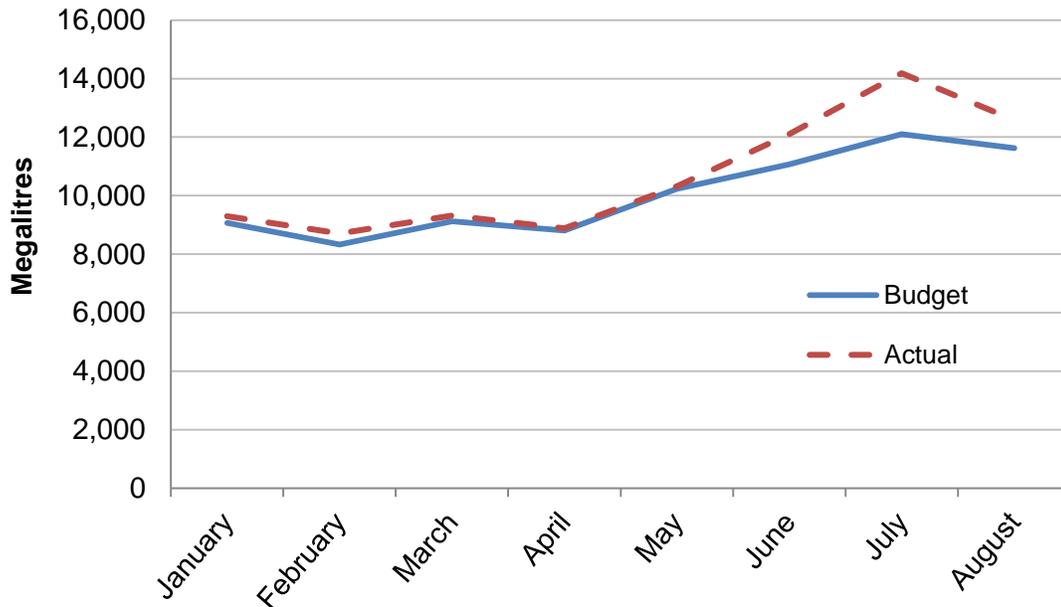
Impact of lower rates in 2020 could be partially offset by higher total consumption and lower expenditures

Water supplied to local municipalities from January to August 2020 was up 6% from budgeted flows, with most of the increase occurring over June to August. Figure 3 shows York Region's bulk water supply to local municipalities, which is largely consumed by residents, and industrial, commercial and institutional (ICI) users.

While the recent uptick in flows is in line with usual fluctuations related to summer weather usage, changes to residential and business activity as a result of COVID-19 may have also affected consumption. Complete information on 2020 flows and the impact on revenue will become available in 2021.

The Region is encouraging local municipalities to analyze their retail data to better determine the impact of COVID-19 on residential and ICI consumption.

Figure 3
York Region Water Supplied to Local Municipalities in 2020



COVID-19 has also affected the Region’s operating expenditures. Water and wastewater expenditures in 2020 so far have been below budget mainly due to recruitment slowdowns and operating efficiencies.

Regional Council’s decision to hold rates at 2019 levels was intended to support residents

Seven of the nine local municipalities made a decision to provide direct rate relief to water and wastewater customers in 2020 in response to COVID-19, with five returning user rates to 2019 levels and two reducing their previously planned increases.

On average, relief measures are expected to provide households in these seven municipalities with about \$15 to \$30 in quarterly savings.

User rate revenue in these municipalities could be up to 10% less than was budgeted in 2020. For municipalities in which information is available, Regional Council’s decision to maintain wholesale rates in 2020 is estimated to offset more than half of the fall in revenues collected.

The previously approved 2.9% rate increase for 2021 aims to balance the shorter-term economic impacts from COVID-19 and the long-term need to achieve full cost recovery

In 2015, Council approved a 2.9% rate increase for April 1, 2021 which was expected to lead to a combined rate of \$3.45 per cubic metre. Because of the deferral of the 2020 increase, reaching this level would now require a 12.2% increase in the current rate.

In spring 2020 the water and wastewater rate model was updated to reflect more current estimates, including for inflation, interest rates, population and future asset management needs. Based on preliminary analysis using the updated model, it was estimated that a rate increase of about 6% for 2021 would achieve full cost recovery while keeping future rate increases at about 2.9% annually.

Uncertainty about the ongoing financial impacts of COVID-19 on ratepayers continues to be an important consideration in setting the 2021 rate. While forecasters are cautiously optimistic about the Canadian and Ontario economy in the medium and longer term, the short-term global impact of COVID-19 is unprecedented in modern times. It is still highly uncertain when residents and businesses in the Region will fully recover financially.

It is recommended that Council continue with a 2.9% increase, leading to a combined rate for April 1, 2021 of \$3.16 per cubic meter. The recommended rate increase is in line with or lower than planned 2021 rate increases to date by most neighbouring jurisdictions.

Full cost recovery could still be achieved in 2021 with the recommended rate increase but maintaining full cost recovery in the future may require annual increases slightly above 2.9%. Staff are updating the rate model through the 2021 User Rate Study and will evaluate options for lowering rate pressure in the near term while ensuring the long-term financial sustainability of the water and wastewater systems.

Known pressures include the need to build reserves for renewal of ageing assets. The Region spent an average of \$75 million per year on water and wastewater rehabilitation projects from 2015 to 2019 and is forecast to spend \$91 million in 2020. This is expected to rise to \$107 million each year, on average, over the remainder of the 10 year plan and continue to increase over the foreseeable future. These reserves can only be maintained at an adequate level after full cost recovery rates are in place.

Rise in the average household bill attributable to the Region's increase is expected to be \$18 in 2021, which is less than estimated 2020 savings

The average annual water and wastewater bill in the Region is expected to rise by \$18 in 2021 (or less than 2.9%), as a result of the recommended increase. Although the wholesale rate that the Region charges is a major component of local water and wastewater budgets, the full impact on household bills will largely depend on the retail rates that are implemented by each local municipality.

Council's decision to not increase the rate in 2020 resulted in about \$57 in average annual savings per household. Overall these 2020 savings are higher than the forecasted \$18 rise in an average household bill, resulting from the Region's recommended increase in 2021. More generally, the average combined water and wastewater bill will remain broadly in line with what households pay for other utilities including electricity and gas.

The 2021 User Rate Study, which will inform Council's decision on rates for 2022 and beyond, will look in more detail at any continued impacts of COVID-19 and the Region's cost pressures. More clarity about the economic picture is likely to emerge as the study is finalized in Q2 2021.

Rate stabilization reserves are available to mitigate the revenue impact in 2020

The Region's rate stabilization reserves are used to manage year-end variances between actuals and the budget. As such, these reserves will be used to offset any revenue shortfall in 2020 driven by the rate deferral. As noted, the estimated \$25 million impact in 2020 from deferring the 9% rate increase assumes flows as per the 2020 Budget. However, the shutdown of businesses and shift to working from home have altered consumption patterns. Summer weather also has an impact on water use, and recruitment slowdowns and operational efficiencies have affected the Region's expenses for 2020. Both of these factors will help to make the final year-end impact less than the \$25 million estimate, which was based on the rate impact alone. Complete information on the impact of these factors will be available in 2021.

Revenue losses in 2021 resulting from the 2020 deferral and other factors may require additional draws from the rate stabilization reserves. This will be considered through the 2021 Budget process.

Establishing 2021 water and wastewater rates supports strategic goals of Vision 2051 and 2019-2023 Strategic Plan

Establishing Regional water and wastewater rates for 2021 supports the Vision 2051 goal of Open and Responsive Governance and the Good Government priority of the 2019-2023 Strategic Plan, particularly the objective of managing the Region's assets for current and future generations.

5. Financial

Use of rate stabilization reserves will minimize 2020 budget impacts

Drawing on rate stabilization reserves to offset lost revenue will minimize the impacts on the budget plan of Council's decision to defer the 2020 rate increase. These reserves were established to mitigate effects of short-term shocks to rates or consumption.

A 2.9% rate increase for 2021 adds pressure on achieving long-term financial sustainability of water and wastewater

As part of the 2021 Budget process, the Region will consider ways to manage any financial pressure that may be created from staying with the planned 2.9% rate increase, including how much to draw from rate stabilization reserves in 2021 to mitigate any shortfalls. Long-term financial sustainability, however, depends on maintaining user rates at a level that builds capital reserves so future asset management needs are met while achieving intergenerational equity and avoiding new user rate debt. The current user rate study will consider this as part of the user rates that it will recommend to Council for 2022 and beyond.

6. Local Impact

Reaffirming the planned water and wastewater user rate increase for the year starting April 1, 2021, would give local municipalities more certainty as they develop their 2021 budgets.

Staff continue to engage with local municipalities to better understand and collaborate on issues of concern to them. Successful roll-out of the previous 2015 rate study was due in large part to educational and promotional materials targeted at ratepayers that explained the benefits of full cost recovery. A similar initiative is being developed for the new study and plan.

7. Conclusion

It is proposed that the Region draw funds from user rate stabilization reserves to offset any revenue shortfall in 2020 associated with deferring the planned 9% increase to the 2020 wholesale rate. Increasing the combined water and wastewater wholesale rate by the previously approved 2.9% for 2021 strikes a balance between the potential ongoing financial impacts of COVID-19 on ratepayers and the Region's goal of full cost recovery.

For more information on this report, please contact Michelle Swan, Director, Business Planning & Operations Support at 1-877-464-9675 ext. 73040 or Kelly Strueby, Director, Office of the Budget at 1-877-464-9675 ext. 71611. Accessible formats or communication supports are available upon request.

Recommended by: **Erin Mahoney, M. Eng.**
Commissioner of Environmental Services

Laura Mirabella, FCPA, FCA
Commissioner of Finance and Regional Treasurer

Approved for Submission: **Bruce Macgregor**
Chief Administrative Officer

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