Background Information

The City of Edmonton owns and operates three utilities: Sanitary, Land Drainage, and Waste Management. The City has provided these utility services for over a hundred years. However, these services have not always been operated under a utility model.

Prior to the adoption of the utility model, tax levy was used to wholly or partially fund the costs of these services. This means that the user fees charged for the services did not necessarily cover the operating and/or capital requirement of the utility systems.

Operating under a utility model, the revenues generated from each of the utilities cover the daily operating costs as well as the long term capital requirements. Under a purely public utility model, the goal is to provide the best possible service at the lowest cost to the customers and return on investment generated from the operation is not a primary consideration. Under a private utility model, utility rates for the services provided are based upon a reasonable, sustainable rate of return on capital investment, governed under regulations of the Alberta Utilities Commission. The City of Edmonton Utilities generally operate under a public utility model; except that it allows for the payment of a dividend to the City of Edmonton based on the actual operating results.

The Sanitary Utility is the most mature of the three utilities, having operated as a full utility since 1956. Currently, it is the only utility that pays a local access fee and an annual dividend to the City of Edmonton. Land Drainage became a utility in January 2003 and its ability to pay a dividend to the City of Edmonton will be reviewed in 2014. Waste Management became a full utility in January 2009 and is exempt from dividend payments at this time. The review and development of a Waste Management Utility Fiscal Policy will determine its ability to pay dividends to the City of Edmonton in the future.

Changes to Budget Process and Documentation

The annual budgets for the Sanitary, Land Drainage, and Waste Management Utilities have traditionally formed part of the overall City of Edmonton Budget. Following the rate setting, governance and regulatory review of the three utilities by HDR Engineering Inc., City Council directed Administration to separate the submission, review and approval of the utility budgets from the City's budget review process. The primary reason for the separation is to allow City Council sufficient time to review and discuss the utility budgets. Accordingly, this document has been prepared for Council consideration on September 25th, 2009, prior to the review of the Corporate Budget in December.

The governance and regulatory review also concluded that as multi-million dollar businesses, Council needs sufficient and appropriate information to make informed decisions. Accordingly, this budget document includes an Overview; Major Services and Activities; Capital Budget Update and Recommended Capital Adjustment; and Supplemental Information.

The Overview is intended to provide sufficient information to demonstrate the business alignment to Council's 30-Year Strategic Goals, a description of the Major Services and Activities, Outcomes and Measures, Issues and Challenges, and the Proposed 2010 Operating Budget summary. This introductory section of the document also outlines Outcomes and Measures. Attached to specific measures and targets, these Outcomes demonstrate the progress of the particular program in relation to the goals set out in The Way Ahead (City of Edmonton Strategic Plan 2009-2018).

The program overview is followed by a description of the Utilities major services. For greater insight, each of the Major Services and Activities include information on Responsibility, Current Service Level, Strategic Initiatives, along with budget information detailing the revenues and expenditures associated with the specific major activity.

Also included is a breakdown of the approved 2009-11 Capital Budget. Where amendments to the approved budget are proposed, the rationale for the adjustment is provided for Council's consideration.

Key Considerations have been identified throughout the document. These major management decisions have been reflected in the Proposed 2010 Budget and are highlighted for Council's consideration.

Finally, to provide full financial information, Supplemental Information is presented in the form of Pro-Forma Statements. The intent of including this information is for completeness purposes; and to present the projected financial picture of the Utilities for the next five years.

Significant Events Affecting the 2010 Budget

The Proposed 2010 Budgets for the three Utilities have been developed by incorporating policies and direction provided by City Council, the current and projected economic conditions and regulatory and contractual commitments made under approved Programs. These are discussed below to provide context for a better understanding of the proposed budget.

Use of Grant Funding

On April 16th, 2008 City Council approved the financial principles for developing the 10 Year Capital Investment Agenda. One of the approved principles is to "Fund utilities [capital] by utility rates". Accordingly, all capital infrastructure requirements by Sanitary, Land Drainage, and Waste Management are now being funded through Utility Rates or third party contributions.

Exceptions are previously approved projects with grant funding that have not yet been completed or new grants that are project based (e.g. Alberta Energy Research Institute grant for Biofuels Facility) as opposed to population-based grants (e.g. Municipal Sustainability Infrastructure).

This direction significantly impacts the rates for the Sanitary Utility customers and will have an impact on the Land Drainage customers within the next couple of years.

From 2005 to 2009, Drainage Services has accessed an average of $15 million annually in grant funding towards its capital requirements. Combined, this represents nearly a 19% rate impact on the drainage utility rates if the capital investment were to be made using cash financing (1% rate represents approximately $600,000 for Sanitary and $200,000 for Land Drainage). If the capital investment were to be financed through 25-year debt, the cumulative impact over a 5-year period is estimated at 1.5%. As will be discussed in the budget document, care needs to be taken in terms of the total debt being carried by the Utilities.

Since 2006, grant financing for capital projects has been mostly directed to the Land Drainage Utility for the Flood Prevention Program implemented as a response to the 2004 storm event. While significantly reduced ($20.7 million budget in 2009), the Land Drainage proposed 2010 budget still contains $7.5 million of grant financing for Capital Projects.

Implementation of Tangible Capital Asset Regulation

The implementation of the required Tangible Capital Asset (TCA) regulation for accounting of capital projects has had a negative impact to both Sanitary and Land Drainage.

TCA is a legislated requirement that comes into effect in 2009. Essentially, it restricts the amount of costs that can be capitalized as part of the capital asset and depreciated over the life of the asset. Implementing this new requirement in the Proposed 2010 Budget has seen an added $1.4 million in expenditure for 2010 that would otherwise have been "deferred".

Sanitary Utility

On March 31, 2009 the City of Edmonton transferred the Gold Bar Wastewater Treatment Plant (GBWWTP) to EPCOR. The budget identifies the portion of revenues collected for the operations and maintenance of GBWWTP separately from the Sanitary Utility. City Administration will present the budget for the wastewater collection and transmission system. Information on the EPCOR budget for GBWWTP is included in the budget documentation. Customers of the Sanitary Utility will continue to see one fee for all sanitary services.

One of the significant events affecting the 2010 Budget is the economic slowdown during 2009, which enabled the Transportation Department to increase the number of pavement overlay neighbourhoods under the Neighbourhood Renewal Program due to lower construction costs. This requires an increase in Drainage Services' capital budget to complete open cut sewer works in more neighbourhoods, ahead of roadway reconstruction or overlay works.

Another significant change to the Proposed 2010 Budget is the financial segregation of Design and Construction, as recommended in the HDR report. Design and Construction currently operates under the

umbrella of the Sanitary Utility. However, it is a non-regulated activity and can be treated as a potential future source of income for the City. The Approved 2009 Budget contained a budgeted transfer of $1.9 million to the Sanitary Utility. This has been reduced to $1.5 million in the Proposed 2010 Budget and is anticipated to be further reduced to $750,000 in 2011.

Land Drainage

As a relatively new utility, Land Drainage is currently exempt from the payment of a local access fee and dividend to the City of Edmonton. This will be reviewed in 2014 as per Policy C304B.

One of the significant factors affecting the Proposed 2010 Budget is the increase in capital investment, such as the Mature Neighbourhood Renewal Program, through debenture debt, which increases the associated interest cost.

A second factor is the lower investment interest rate which reduces the amount of interest revenue available to offset increased costs.

Waste Management Utility

After an additional 10 years capacity made possible by a commitment to waste reduction and diversion from landfill through recycling and composting, the Clover Bar Landfill finally reached capacity after serving Edmonton and region for 35 years and closed in August 2009. The landfill closure necessitates a significant change to the waste management operations as long distance hauling to Ryley significantly increases the cost of disposal. This cost pressure on Waste Management is expected to continue through to 2013.

In preparation to mitigate the amount of long distance hauling required, efforts have been underway for the past number of years to decrease the amount of waste material being sent to the landfill. Currently, Edmonton has achieved a 60% diversion of its residential waste through reduction, recycling and composting initiatives.

The GEEP electronic and electrical waste recycling facility, the commissioning of the Biofuels Facility (expected in late 2011), and the commissioning of the Greys Paper Recycling Facility (expected by early 2011) are expected to further increase the residential waste diversion rate from landfill to 90% .

In addition, efforts are underway to enhance construction and demolition waste recycling to act on potential new revenue opportunities and further reduce the amount of materials being hauled to Ryley .

Another cost pressure that would need to be addressed in future budgets is the treatment of depreciation on the integrated waste collection and disposal system. With the move to full utility and the legislated changes surrounding Tangible Capital Assets, depreciation associated with the capital investment that was not previously included in the rate structure will now have to be addressed. Council will provide direction on the treatment of depreciation as part of the Waste Management Fiscal Policy planned for review by Council in early 2010.

Prior Commitments

When City Council approved the 2009 Budgets for the three utilities, Administration indicated that the three-year rate increases needed were as follows:

	2009	2010	2011
Sanitary Utility	8%	8%	8%
Land Drainage	8%	8%	8%
Waste Mgmt	$26.59	$34.50	$36.94

Despite some of the unexpected events impacting the utilities, the Proposed 2010 Budget reflects an 8% increase to both the Sanitary and Land Drainage Utilities; however, the projected Net Income is lower than in prior years. The Waste Management Utility was able to reduce its projected increase from $34.50 to $29.85 as a result of steps that were undertaken during 2009. These are discussed in the Waste Management section of the document.

Impact on Typical Household

The Proposed 2010 Budgets do include an increase to the utility rates, as outlined in the table below.

	Average Monthly Usage	2009		Proposed 2010		Increase*
		Rate	Monthly Charge	Rate	Monthly Charge	
Sanitary	17.5 m^3	\$5.64 + \$1.077/m^3	\$ 24.49	\$6.09 + \$1.163/m^3	\$ 26.44	\$ 1.95 (8.0%)
Land Drainage	average residential lot size (592 m^2)	\$0.0186/m^2 with run-off co-efficient of 0.5	\$ 5.51	\$0.0201/m^2 with run-off co-efficient of 0.5	\$ 5.95	\$ 0.44 (8.0%)
Waste Management	single family	\$ 26.59	\$ 26.59	\$ 29.85	\$ 29.85	\$3.26 (12.3%)
Total			**\$ 56.59**		**\$ 62.24**	**\$5.65 (10.0%)**