



EPCOR Water Services - PBR Timeline and Guiding Principles

RECOMMENDATION

That Utility Committee recommend to City Council:

That the regulatory schedule and guiding objectives, as set out in Attachment 1 of the May 6, 2024, EPCOR Water Services Incorporated report EXT02465, to assess the performance based regulation rates application to establish new rates for wastewater collection and wastewater treatment, effective April 1, 2025, be approved.

Report Purpose

Council decision required.

Executive Summary

- By June 2024, EPCOR Water Services Inc. (EWS) will be submitting its Performance Based Regulation (PBR) Rates Application for approval by City Council to establish customer rates for Wastewater Collection (previously referred to as “Drainage Services”) and Wastewater Treatment services for the period April 1, 2025 to December 31, 2027.
- This report provides an overview of performance based regulation and the proposed regulatory process for Utility Committee and City Council to assess the reasonableness of the EWS’ PBR Application. The process includes the review by Utility Committee of the PBR Application and submissions from Administration, the Utility Advisor, and the public at the October 11, 2024, Utility Committee meeting.

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REPORT

Background

EPCOR Water Services Inc. (EWS) provides water, wastewater treatment and wastewater collection services (previously referred to as “drainage services”) to the City of Edmonton. The City of Edmonton has franchise agreements with EWS that grant EWS the exclusive right to provide these services within the boundaries of the City of Edmonton. As a regulated utility, EWS is subject to regulation to ensure services are provided at a fair price and that appropriate service levels are maintained. City Council maintains regulatory oversight responsibility for the water, wastewater treatment and wastewater collection utilities owned and operated by EWS.

The *Public Utilities Act and Municipal Government Act* provide City Council with the authority to pass bylaws relating to municipal public utilities, including those owned and operated by municipally controlled corporations, and to set terms, costs, or charges relating to those public utilities within the boundaries of the City of Edmonton. As regulator, City Council is expected to balance the interests of the customers (high quality and reliable services at reasonable costs) with the interests of EWS (financially sustainable utility that provides fair investment returns).

City Council has approved separate bylaws to establish the customer rates and terms and conditions of service under Performance Based Regulation (PBR) for each of EWS’ Water Services, Wastewater Collection Services and Wastewater Treatment Services. City Council approved Bylaw 19626 on August 30, 2021 that sets customer rates for water services charged by EWS for the five year period April 1, 2022 to March 31, 2027.

City Council also approved Bylaw 19627 - EPCOR Drainage Services and Wastewater Treatment Bylaw (Bylaw 19627) on August 30, 2021 that sets customer rates for wastewater treatment and drainage services charged by EWS for the three year period April 1, 2022 to March 31, 2025. This was the third PBR term for wastewater treatment services and the first PBR term for drainage services.

Bylaw 19627 that sets customer rates for EWS’ wastewater services (wastewater collection and wastewater treatment) is set to expire on March 31, 2025. Therefore, new or amending Bylaw is required to set fees, rates and charges to be effective April 1, 2025. This report outlines the regulatory process and schedule to establish new rates for EWS’ wastewater services, effective April 1, 2025.

Overview of Performance Based Regulation

One of the guiding principles used in establishing fair rates is that “all customer charges will be based upon cost of service”. A cost of service approach is the most common method to

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determine regulated utility rates. Under a traditional cost of service approach, rates are generally established by the regulator every one to two years through a two-phase process.

In the first phase, the regulator determines the total amount of money (“revenue requirement”) required by the utility to provide its regulated services in a year. The revenue requirement is comprised of the forecast costs required to operate, maintain and invest in the utility system plus a fair return on the utility’s investment (return on equity). The return on equity also compensates the utility for the risks inherent in operating the business.

In the second phase, individual customer rates are established that will allow the utility to recover the total annual revenue requirement. A cost of service analysis is first completed to determine how much of the total revenue requirement should be equitably recovered from each customer class (e.g. residential, commercial). A rate design analysis is then completed to determine how the individual customer rates should be designed and structured to recover the revenue requirement allocated to each customer class (e.g. fixed vs variable).

Under a PBR approach, customer rates are determined for the first year of the term based on the cost of service two phase approach described above. The customer rates are then adjusted in each subsequent year by a predefined formula (I-X) for the term of the PBR plan. The basic formula adjusts customer rates annually by a rate of inflation (“I”) that reflects the increased cost of labour and non-labour inputs the utility uses, which is then reduced by an efficiency factor (“X”) to reflect the productivity improvements the utility can be expected to achieve during the PBR period.

Generally, the utility bears the risk of normal factors that could impact revenues and costs above the inflation and efficiency factors (I-X) (e.g. weather, consumption). However, extraordinary or uncontrollable factors that have a significant impact and are beyond the control of the utility may be eligible for a “non-routine” rate adjustment and flowed through to customers (e.g. legislative changes).

Establishing customer rates under a PBR approach creates stronger incentives for the utility to improve its efficiency through cost reductions and other measures since it is able to retain the increased profits from these measures for a longer period than it would under a traditional cost of service approach. At the same time, customers automatically share in the expected efficiency gains because they are built into rates through the efficiency factor, regardless of the actual performance of the utility. Other benefits include customers receiving stable and predictable rates over a longer term (e.g. five years) and a reduction in the frequency and cost of regulatory applications being filed and approved (“regulatory burden”).

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EWS' 2025-2027 Wastewater PBR Application

EWS will be submitting its PBR application by June 2024 for approval by City Council to establish customer rates under PBR for wastewater services for the three year period April 1, 2025 to December 31, 2027. EWS then plans to submit a consolidated PBR application for all three operations in 2027. To enable the submission of a consolidated PBR application for all three operations of EWS (namely, Water, Wastewater Collection, and Wastewater Treatment), the 2025-2027 PBR term will be shortened by three months. The term of this consolidated PBR application will commence on January 1, 2028, enabling EWS to schedule future rate changes to take effect on January 1st of each year rather than April 1st.

The main elements of the 2025-2027 Wastewater PBR application to set customer rates effective April 1, 2025 will include the following:

- A mechanism to adjust customer rates, fees and charges annually under a performance based regulation formula (e.g. I-X);
- A mechanism for non-routine adjustments under the performance based regulation framework, similar to Bylaw 19627 for drainage services and wastewater treatment services;
- Terms and Conditions of service; and
- Service quality metrics and targets, detailed in a similar manner Bylaw 19627 for drainage services and wastewater treatment services.

Regulatory Process and Timelines

A comprehensive regulatory process is followed by City Council in the review and approval of utility customer rates for EWS, and is similar in many respects to the approach used by other Provincial regulatory bodies, including the Alberta Utilities Commission. Administration has reviewed the proposed timelines in Attachment 1 for Utility Committee and City Council to review and approve the performance based rates applications for wastewater services to set customer rates effective April 1, 2025. Key dates and milestones include the following:

May 31, 2024	PBR Application submitted to the City Manager
July 15, 2024	Written questions to EWS from Councillors, Utility Advisor and Administration
July 22, 2024	Written questions to EWS from the Public
August 5, 2024	Written responses from EWS to questions from Councillors, Utility Advisor, Administration and the Public
September 4, 2024	Reports from Administration and the Utility Advisor

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October 11, 2024	Utility Committee meeting to review PBR application and submissions from EWS, Administration, Utility Advisor, and the Public. Recommendation to City Council approving the PBR rates application and applicable bylaws
November 2024 – January 2025	City Council approval of PBR rates application and three readings of applicable bylaws

The proposed process and schedule outlined in Attachment 1 is consistent in most respects to the regulatory process followed in 2021 for the approval of EWS' PBR applications (Wastewater Treatment and Drainage Services 2022-2024) and (Water Services 2022-2026). The guiding objectives used in the past for assessing EWS' proposed rates have also been included in Attachment 1.

ATTACHMENT

1. 2025-2027 PBR Application – Proposed Regulatory Schedule and Guiding Objectives