

EPCOR Water Services Inc. - Water, Wastewater and Drainage Based Rates Process and Timeline Report

Recommendation

That the October 2, 2020, Financial and Corporate Services report CR_8146, be received for information.

Executive Summary

This report provides an overview of the approach proposed by EPCOR Water Services Inc. to submit performance based regulation applications in early 2021 and request approval from City Council to establish rates for water services for the period April 1, 2022 to March 31, 2027, and rates for wastewater treatment and drainage services for the period April 1, 2022 to March 31, 2025. The report also provides an update on potential enhancements that may be implemented to further improve the regulatory process and to assist the Utility Committee with the effective review of the significant volume of information based on EPCOR Water Services Inc.'s proposed approach.

Report

EPCOR Water Services Inc. (EWSI) has provided a Process and Timeline report (Attachment 1) to obtain feedback from the Utility Committee on its proposed approach for preparing Performance Based Regulation (PBR) applications and obtaining City Council approval to establish customer rates beginning April 1, 2022 for each of water, wastewater treatment and drainage services. The PBR terms under which EWSI is currently providing these services within the City of Edmonton are set to expire on March 31, 2022. On October 25, 2016, City Council approved Bylaw 17698, which sets customer rates for water and wastewater treatment services charged by EWSI under PBR for the five year period from April 1, 2017 to March 31, 2022. On September 12, 2017, City Council also approved Bylaw 18100, which sets customer rates for drainage services provided by EWSI under PBR from January 1, 2018 to March 31, 2022.

Process and Timeline Report - Overall Approach

At the June 9, 2017 Utility Committee meeting, Administration presented a number of potential enhancements to the current regulatory process used to establish customer rates for EWSI that were discussed in report CR_4188. In particular, Administration

highlighted that the transfer of drainage services to EPCOR required separate regulatory proceedings and PBR terms that are staggered for water, wastewater treatment, and drainage services. This would reduce the regulatory burden and allow EWSI to prepare, and to give City Council, Utility Committee, and Administration the opportunity to effectively review the comprehensive rate applications. EWSI had initially suggested combined drainage and wastewater treatment PBR applications could be submitted for the five year term April 1, 2022 to March 31, 2027. The existing PBR term for water services would then be extended two additional years to March 31, 2024 based on a smaller application to update rates, performance targets and the capital program for the interim two year period. A subsequent water PBR application would be made for the period April 1, 2024 to March 31, 2029.

EWSI has since reviewed the implications of potentially extending the PBR term for water services for an additional two year period and has concluded that this is no longer a viable approach. The customer rates as established under the existing PBR formula will not adequately address the forecast capital program or other inflationary pressures EWSI expects to incur in 2023 and 2024. Therefore, EWSI is proposing that full PBR applications be submitted for each of water, wastewater treatment and drainage services to establish customer rates, effective April 1, 2022. To stagger the PBR terms and future regulatory proceedings, EWSI is recommending that the water services application be for a five year term effective April 1, 2022 to March 31, 2027, with the drainage and wastewater treatment applications being aligned for a three year term of April 1, 2022 to March 31, 2025 and subsequent PBR applications for the period April 1, 2025 to March 31, 2030.

Although the proposed approach of submitting full PBR applications for water, wastewater treatment and drainage services effective April 1, 2022 will significantly increase the regulatory burden in 2021, Administration considers the approach to be supportable to the extent that:

- the PBR formula and underlying capital and operating programs for Drainage services under Bylaw 18100 should be evaluated and reset since the initial PBR term is ending under which drainage assets were transferred to EWSI; and
- EWSI has indicated that the existing PBR formula for water services under Bylaw 17698 will no longer allow EWSI to adequately recover its costs and earn a reasonable margin of profit; this is a guiding objective for establishing rates, per Bylaw 12294 EPCOR Edmonton Regulated Utilities Procedures.

EWSI met with the Utility Advisor and Administration in early 2020 to begin discussions on the proposed approach and other alternative methods that could be used to set customer rates in an efficient and effective manner. Administration notes that EWSI has since evaluated whether certain elements of the existing PBR formula under Bylaw 17698 could be modified in a relatively simple and straightforward manner to

allow for the existing water PBR term to be extended an additional two years, but concluded that this was also not a feasible approach.

Process and Timeline Report - Specific Regulatory Issues

EWSI has identified a number of specific matters in Attachment 1 for the upcoming PBR applications that it is requesting initial feedback from the Utility Committee on including the allowed return on equity, efficiency factor (productivity improvements EWSI can be expected to achieve during the PBR term), rate design for water services, cost of service and billing discrepancies for drainage services, and the potential implementation of Automated Metering Infrastructure.

In approving the 2017-2021 water and wastewater treatment PBR applications in the fall of 2016, the Utility Committee noted the lack of balanced expert testimony for establishing the appropriate return on equity and efficiency factor. Historically, EWSI provides expert testimony for return on equity and efficiency factor as part of its comprehensive PBR application, whereas Administration engages an external consultant to review and provide comments on the overall application but not individual experts for specific technical matters given the cost of obtaining such reports. Over the past several months, EWSI and Administration have been working collectively to determine if a cost effective and balanced approach could be identified for providing expert information on setting the appropriate return on equity (e.g., linked to the Alberta Utilities Commission approved return on equity for regulated utilities in Alberta) and efficiency factor. A common approach has not been identified to date for return on equity based on the limited interest and response from industry experts. As an alternative, EWSI is evaluating how it can further supplement its traditional return on equity evidence to incorporate the feedback received from the Utility Committee. EWSI and Administration continue to work towards a common approach for establishing the efficiency factor.

PBR Regulatory Process - Potential Enhancements

As noted in CR_4188, a comprehensive regulatory process is currently followed in the review and approval of utility customer rates for EWSI, and is similar to the approach used by other Provincial regulatory bodies including the Alberta Utilities Commission. This approach includes:

- Performance Based Regulation that creates incentives for EWSI to improve efficiency while reducing the number of regulatory proceedings and burden;
- comprehensive PBR Rate Applications prepared in accordance with minimum filing requirements resulting in a significant level of information being provided;
- responses from EWSI to Information Requests from Administration, the Utility Advisor and Councillors; and

- a Public Hearing to allow the Utility Committee to further review submissions from EWSI, Administration, the Utility Advisor, and other interested persons, and to obtain additional responses to questions on key issues.

A number of potential enhancements to the current regulatory process that were discussed at the June 9, 2017 Utility Committee meeting have also been implemented. These include a regulatory training session in February 2018 to provide Utility Committee members with a further understanding of utility rate setting principles, removing the restriction that members can only be re-appointed to the Utility Committee for successive terms totalling not more than eight consecutive years, increasing the regulatory capacity in Administration, and enhanced ongoing and periodic reporting to the Utility Committee and public awareness and engagement by EWSI.

A draft schedule for the upcoming PBR applications is provided on page 13 of Attachment 1, which incorporates the process and timeline requirements as prescribed under EPCOR Edmonton Regulated Utilities Procedures Bylaw 12294. Administration is assessing potential amendments to Bylaw 12294 and other enhancements that may further improve the regulatory process given the significant volume of information that will be submitted by EWSI in February 2021. These include:

- Administration releasing its Reasonableness Review report of the PBR rates applications (including EWSI responses to information requests) further in advance of the Public Hearing;
- moving the deadline for Councillors/Committee members to submit written questions on key issues to later in the regulatory schedule rather than within seven working days of the 1st reading of the Bylaw by City Council (potentially after the Administration Reasonableness Review report is released); and
- amending the procedural format of the public hearing to suspend the five minute limitation to allow Utility Committee members to ask a longer series of questions within a single topic, to allow for a more structured final response by EWSI to key issues discussed, and to provide additional time for the Utility Committee to deliberate on the issues and final motion to Council on the PBR applications.

Administration is also reviewing whether the first reading by City Council of the proposed Bylaw to set customer rates should be moved from the beginning of the regulatory process (in accordance with Section 8 of Bylaw 12294) to the end of the process after the Utility Committee has completed its deliberations and given final direction on the PBR applications. This change would allow EPCOR and Administration to more efficiently amend the PBR applications and proposed rates Bylaw to reflect the final decisions and recommendations of the Utility Committee prior to going to City Council for any further deliberations and final approval.

Next Steps

Based on feedback received at the October 2, 2020 Utility Committee meeting, Administration will continue to work towards implementing these and other enhancements in advance of the PBR applications being submitted by EWSI in February 2021. This includes Administration returning with an amended EPCOR Edmonton Regulated Utilities Procedures Bylaw 12294 for recommendation by Utility Committee and approval by City Council in December 2020.

Budget/Financial Implications

EWSI notes in section 6.4 of Attachment 1 that it began an audit of the Stormwater utility in 2019 that identified a number of billing discrepancies and inconsistencies. EWSI is continuing to investigate and address these discrepancies to achieve equity and fairness across all stormwater utility ratepayers and avoid cross subsidization. Further to this, EWSI will be proposing an increase in the stormwater fees charged to the City of Edmonton effective April 1, 2022 as part of the upcoming Drainage services PBR application. These rates will be reflected in the updated cost of service study and subject to the Reasonableness Review by City Administration.

EWSI indicates that the City of Edmonton is the largest stormwater utility customer and, based on the guiding principles for establishing equitable rates, the City should be paying approximately \$680,000 per month rather than the current amount of \$88,000 per month. EWSI is prepared to work with the City to ensure a smooth implementation of these additional charges. The impact of this proposed change would be an increase in the operating budget and potentially the tax levy for the City of Edmonton to cover these additional charges with a corresponding decrease in stormwater fees paid by other EWSI customers.

Corporate Outcomes and Performance Management

Corporate Outcome(s): The City of Edmonton has sustainable and accessible infrastructure.			
Outcome(s)	Measure(s)	Result(s)	Target(s)
Ongoing monitoring and reporting of EPCOR utility services regulated by City Council.	Annual and periodic reporting of utility operations.	Annual Progress Report - Water, Wastewater, Drainage (June 2019) Annual Operational Plan (February 2019)	Annual Progress Report - Water, Wastewater, Drainage (June) Annual Operational Plan (Q1)

Attachments

1. EPCOR Water Services Inc - Performance Based Regulation Renewal Process and Timeline Report

Others Reviewing this Report

- G. Cebryk, Deputy City Manager, City Operations
- J. Meliefste, Acting Deputy City Manager, Integrated Infrastructure Services
- R. Smyth, Deputy City Manager, Citizen Services
- S. McCabe, Deputy City Manager, Urban Form and Corporate Strategic Development
- B. Andriachuk, City Solicitor