

Non-regulated Loan Repayment Plan

Recommendation

That the December 4, 2020, City Operations report CR_8447 be received for information.

Executive Summary

Through the City's Program and Service Review and the 25-year Waste Strategy work, it was determined that the City's involvement in the non-regulated business lines was assessed as inadequate both in terms of achieving diversion and financial results.

To address non-regulated program losses and achieve target cash balances, the Waste Services Utility was given authorization, through the 2015 Operating Budget process, to draw on a notional short-term loan from the City of Edmonton. The notional short-term loan was available from 2015 to 2019. Access to this notional loan ensured that losses from the non-regulated lines of business were financed by the notional loan and did not impact regulated rate revenue. This report outlines various options for repayment of the notional short term-loan to the City. Administration will return in 2021 with a recommended repayment option for the notional loan.

Report

Background

Waste Services is legislated to provide services for single unit and multi-unit residential properties within city limits, which are the regulated activities of the Utility. The City of Edmonton is not required to offer non-regulated waste services, but has been active in this space since 2008, seeking to improve diversion rates in the non-regulated sectors.

As part of the 25-year Waste Strategy, an assessment of the City's non-regulated business lines was conducted to determine whether participation in non-regulated business activities is the most effective way to influence diversion in these sectors. An extensive preliminary review of the business lines was also conducted by the City's Program and Service Review in 2018, which assessed the City's four non-regulated business lines:

1. Commercial Collections
2. Commercial Self-Haul
3. Construction and Demolition Processing
4. Aggregate Recycling

Building on the work from the Program and Service Review, public engagement was conducted as part of the strategy to seek clarification from a variety of organizations on the ways the City can most effectively and efficiently impact waste reduction and diversion in the non-residential sectors.

It was determined that the City's involvement in direct collection of waste from the Industrial, Commercial and Institutional sector has been inadequate in its efforts to impact waste diversion in the non-regulated sectors. While the business line has successfully grown a modest client base, its impacts are only felt on approximately four percent of the industry. Only a small number of City clients have been able to fully participate in waste diversion programming, which was challenged further with the closure of the Edmonton Composting Facility.

The 25-year Waste Strategy recommended changes to the City's current non-regulated business lines, including a wind-down of the Commercial Collections business and securing an operational partner for the Construction and Demolition Recycling business. The City's involvement in these business lines was assessed as inadequate in terms of achieving both diversion and financial results. More information and details are provided in the August 29, 2019 City Operations report CR_5829, Attachment 4. Council approved the recommendation to exit and wind down these two lines of business in September 2019.

After Council's approval, Waste Services proceeded with securing an operational partner for the Construction and Demolition business. The Construction and Demolition Recycling Facility has been managed and operated by an independent contractor since April 2020. The Commercial Collections business is expected to fully wind down by the end of 2021, with the exception of City of Edmonton facilities and some mixed-use sites.

Non-Regulated Program Plan

To address non-regulated program losses and achieve target cash balances, the Waste Services Utility was given authorization through the 2015 Operating Budget process to draw on a notional short-term loan from the City of Edmonton. The notional short-term loan was available from 2015 to 2019. Access to this notional short-term loan ensured that losses from the non-regulated lines of business were financed by the notional loan and did not impact regulated rate revenue.

As of December 31, 2019, the notional short-term loan has provided financing for the \$9 million of cumulative losses generated by the non-regulated lines of business, and no further losses are forecast at this time. Waste Services conducted a financial review of five potential notional loan repayment options. The options are described in more detail below.

1. Repayment utilizing non-regulated profits
2. Transfer of Stranded Assets to Tax Supported Operations
3. Full notional loan forgiveness
4. Repayment utilizing unappropriated retained earnings of the utility
5. Interest only payments for five years starting in 2021 and re-evaluate the repayment options in 2026 based on financial sustainability of the non-regulated business lines

1. Repayment Utilizing Non-regulated Profits

Modest profits are anticipated to be generated by the remaining two non-regulated lines of business. These profits could be used to pay down the balance of the notional loan starting in 2021. Future profits expected to be generated by the remaining non-regulated business lines is estimated to be approximately \$0.5 million annually. It is estimated that the notional loan will be fully repaid by 2041 using these profits. Interest on the outstanding notional loan balance will accrue annually at 1.5 percent until the notional loan is fully repaid.

2. Transfer of Stranded Assets to Tax Supported Operations

Under the stranded asset transfer option, the stranded capital assets primarily associated with the non-regulated construction and demolition and Commercial Collections lines of business that received approval to wind down in 2019 would be transferred to the tax levy at the end of 2020. This would reduce the amount of amortization and interest expense covered by the non-regulated business (approximately \$500,000 annually), resulting in higher overall profits generated by the remaining non-regulated lines of business, and would allow the notional loan to be repaid sooner. It is estimated that the notional loan will be fully repaid in approximately eight years under this option with repayment starting in 2021. Net profit from non-regulated lines of business would transfer over to the tax levy until the notional loan is fully repaid.

3. Full Notional Loan Forgiveness

The full amount of the notional short-term loan would be written off to the tax levy. This would be immediate in nature. Revenue from non-regulated operations, less an amount to fund the Industrial, Commercial and Institutional (ICI) program, would transfer over to the tax levy. This transfer of revenue would be indefinite.

4. Repayment Utilizing Unappropriated Retained Earnings of the Utility

The notional loan would be repaid using unappropriated retained earnings of the Utility over a period of five years. The non-regulated business lines have experienced cumulative losses of \$9 million as of December 31, 2019, and have not contributed to the unappropriated retained earnings of the Utility. Repayment of the notional loan

using retained earnings generated by the regulated lines of business would result in regulated customers subsidizing the non-regulated lines of business.

5. Interest Only Payments and Re-evaluate Repayment Options at Later Date

A fixed amount would be paid by the Utility equal to the interest accrued on the notional loan. The expected interest rate is 1.5 percent per annum, and the balance is approximately \$9 million. The amount of interest payment would be \$135,000 per year. This payment would begin at the start of 2021 and end at the end of 2025. Repayment options would be re-evaluated at that time based on the financial sustainability of the non-regulated business lines.

The table below shows a summary of each option.

Repayment Options*	1	2	3	4	5
Notional Loan Amount	\$9,067,000	\$9,067,000	\$0	\$9,067,000	\$9,067,000
Estimated Annual Notional Loan Payment	\$500,000	\$1,076,000	\$1,076,000	\$9,067,000	\$150,000
Payback Period (Years)	18	8	NA	1	5 years + TBD

*Assumes \$250,000 in annual funding will be required to support the engagement and development of the Industrial, Commercial and Institutional (ICI) program.

Next Steps

Administration will return to the Utility Committee in 2021 with a recommended option for notional loan repayment based on the 2020 year end financial position of both the City of Edmonton and the Waste Services Utility.

Corporate Outcomes and Performance Management

Corporate Outcome(s): The City of Edmonton has a resilient financial position.			
Outcome(s)	Measure(s)	Result(s) 2020 Budget	Target(s) 2021 Proposed
Edmonton's waste service rates and fees are fair, equitable and value-driven.	Annual Net Income (\$000s)	6,571	5,280
	Stable Rates	0.3%	0%

Non-regulated Loan Repayment Plan

	Debt to Net Assets Ratio	78.1%	77.7%
	Cash Position (\$000s)	86,013	31,107

Others Reviewing this Report

- M. Persson, Deputy City Manager and Chief Financial Officer, Financial and Corporate Services
- C. Owen, Deputy City Manager, Communications and Engagement
- B. Andriachuk, City Solicitor