

Clause No. 4 in Report No. 10 of Committee of the Whole was adopted, without amendment, by the Council of The Regional Municipality of York at its meeting held on May 15, 2014.

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**MUNICIPAL REQUIREMENT OF SAFE DRINKING WATER ACT, 2002
- WATER FINANCIAL PLAN**

Committee of the Whole recommends adoption of the following recommendations contained in the report dated May 8, 2014 from the Commissioner of Environmental Services:

1. RECOMMENDATIONS

It is recommended that:

1. Council approve the Water Financial Plan (*Attachment 1*) prepared for York Region's Municipal Drinking Water System (License number 013-301A), in accordance with Ontario Regulation 453/07.
2. Environmental Services staff submit the Water Financial Plan to the Ministry of the Environment and Ministry of Municipal Affairs and Housing in accordance with the *Safe Drinking Water Act, 2002*.
3. Environmental Services staff issue notice of the Water Financial Plan availability, as prescribed by Ontario Regulation 453/07, in the local media and on the Region's website.

2. PURPOSE

This report seeks Council authorization of the Municipal Drinking Water System Financial Plan prepared as a requirement under the *Safe Drinking Water Act, 2002*.

The Water Financial Plan outlines the processes in place within York Region to ensure the long-term financial sustainability of the drinking water system, as well as funding for new infrastructure and existing infrastructure maintenance. The Water Financial Plan documents financial commitments and funding sources for the current budget year, commencing with York Region's 2014 budget, and projections for the subsequent six years, including both capital and operating expenditures.

The 2013 State of Infrastructure Update report (also on this agenda) provides a snapshot of the Region's assets with a short-term outlook. The financial grades in the 2013 State of Infrastructure Report represent the current reserve balances for capital replacement only, whereas York Region's Water Financial plan provides a long-term view of the financial sustainability of the water system.

3. BACKGROUND

Water Financial Plan required under the *Safe Drinking Water Act, 2002*

As part of the Province's commitment to fulfill Justice O'Connor's Walkerton Inquiry recommendations, the Ministry of the Environment (MOE) implemented an approvals framework under the *Safe Drinking Water Act, 2002* for municipal residential drinking water systems called the Municipal Drinking Water License Program. All municipal residential systems must be licensed under the municipal drinking water licensing program.

Justice O'Connor recommended that owners of municipal water systems obtain a license for the operation of their drinking water systems. The license is issued to owners by the MOE under the *Safe Drinking Water Act, 2002* once the owner demonstrates it has the following five elements in place:

1. Drinking-water works permit
2. Permit to take water
3. Approved operational plan
4. Accredited operating authority
5. Approved financial plan

Having met all of the necessary prerequisites, the Ontario Ministry of the Environment issued York Region a Municipal Drinking Water License for its drinking water system on January 29, 2010. As of September 2011, all existing municipal residential drinking water systems in Ontario had received a license and a drinking water works permit.

York Region required to submit a renewal application for Municipal Drinking Water License every five years

Municipal drinking water licenses are valid for five years; however, the *Safe Drinking Water Act, 2002* requires an expiry date and renewal application deadline to be included in every license. To ensure that a license remains valid, municipalities are required to submit a renewal application on or before the date listed in Schedule A of their license; for York Region this date is July 29, 2014.

Council endorsement of York Region's Water Financial Plan required before submission due date of July 29, 2014

The information to be submitted for a license renewal is essentially the same as the information required for the issuance of the first license except updated Financial Plans are required to be prepared and approved by Council resolution, in addition to assurance that the system has been and will continue to be operated in accordance with the requirements under the *Safe Drinking Water Act, 2002* and the license.

Work is currently underway to prepare and/or update the required five elements (mentioned above) to support the July 2014 submission of the license renewal application. The Region's Drinking Water Works Permit, Permits to Take Water, and Drinking Water Quality Management Standard (DWQMS) operating accreditations are current and up-to-date. The DWQMS Operational Plan was last endorsed by the Commissioner of Environmental Services in December 2008. Updates to the Operational Plan are in progress and will be submitted to the Commissioner of Environmental Services for endorsement at the end of May 2014.

Regulatory requirements include making Financial Plan available to those served by the drinking water system

The detailed Water Financial Plan, completed by staff in accordance with the regulatory requirements (as listed below), is included as *Attachment 1* to this report.

Ontario Regulation 453/07 s.30(1) Part b of the *Safe Drinking Water Act, 2002* details the requirements for drinking water license renewals, including the need to prepare a financial plan that:

- Is approved by Council resolution (or governing body)
- Applies to a period of at least six years
- Begins with the year that the licence expires
- Provides notice to the public on its availability
- Is made available, upon request, to members of public served by the drinking water system without charge
- Is made available through publication on the Internet at no charge
- Ensures copies are given to the Ministry of Municipal Affairs and Housing

In addition to the above requirements, financial plans must include the following details which are summarized in Table 1:

Table 1
Detailed Financial Plan Requirements

Summary of Required Details	Detailed Breakdown
Proposed or projected financial position of drinking water system	<ul style="list-style-type: none"> • Total financial assets and liabilities • Net debt • Non-financial assets that are tangible capital assets • Tangible capital assets under construction • Inventories of supplies and prepaid expenses • Changes in tangible capital assets that are additions, donations, write downs and disposals
Proposed or projected financial operations of drinking water system	<ul style="list-style-type: none"> • Total revenues (further itemized by water rates, user charges and other revenues) • Total expenses (further itemized by amortization expenses, interest expenses and other expenses) • Annual and accumulated surplus or deficit
Proposed or projected gross cash receipts and gross cash payments	<ul style="list-style-type: none"> • Operating transactions (cash received from revenues, cash paid for operating expenses and finance charges) • Capital transactions (proceeds on the sale of tangible capital assets and cash used to acquire capital assets) • Investing transactions (acquisition and disposal of investments) • Financing transactions (proceeds from the issuance of debt and debt repayment) • Changes in cash and cash equivalents during year • Cash and cash equivalents (beginning and end of year)

4. ANALYSIS AND OPTIONS

York Region's Water Financial Plan prepared in accordance with Ministry of the Environment financial plan regulations

York Region's Water Financial Plan has been prepared in accordance with Ministry of the Environment requirements to report using full accrual accounting, which recognizes revenues and expenditures in the same period as the activities that give rise to them regardless of when they are actually paid for. Since an exchange of cash is not necessary to report a financial transaction, the accrual method is meant to provide a more accurate picture of a municipality's financial position.

In May 2011, Council approved a combined 10 per cent annual rate increase for water and wastewater for 2012 to 2015. The Water Financial Plan was prepared using these approved rate increases up to 2015. For subsequent years, a nine per cent yearly water rate increase was assumed.

Throughout the balance of 2014 and 2015, a comprehensive water and wastewater rate study will be completed that will address requirements for rate stability while maintaining a balance that encourages wise use of water. This study will inform the rates and rate structure that will be presented to Council for endorsement in 2015 for the time period beginning April 2016.

Pricing structures that support conservation and full cost recovery will achieve benefits over the long-term

The Value of Water initiative is a comprehensive approach to increase public awareness on the importance and value of water in coordination with a financial review of water cost models. These initiatives have built, and continue to build, on the success of the *Water for Tomorrow* program and the Long Term Water Conservation Strategy by driving conservation efforts while ensuring adequate funding is available for rehabilitation and replacement of water and wastewater infrastructure. This initiative will also provide input to wholesale water and wastewater rate recommendations in 2015.

Full cost recovery involves thorough life-cycle analysis of costs

Full cost recovery is the first step in the analysis of a water conservation-oriented price structure. Determining full cost recovery involves a thorough life-cycle analysis of costs for the operation of the water supply and treatment system. Subsequent to determining the threshold for full cost recovery, an evaluation of conservation-based pricing structures including tiered block rates, seasonal rates and water budgeting will be conducted. Alternative pricing structures will be evaluated to determine ability to:

- Reduce water consumption without negative impacts on municipal revenues
- Recognize the efforts of customers in choosing water efficient products and practices
- Target inefficient and discretionary potable water uses, such as landscape irrigation
- Delay costly water supply expansion projects
- Avoid financial burdens on industrial, commercial, institutional and low income customers
- Ensure revenue stability that is consistent with forecasts

***Safe Drinking Water Act, 2002* requires a declaration of the financial plan's sustainability**

The *Safe Drinking Water Act, 2002* requires a declaration of the financial plan's sustainability but it does not give a clear definition of what would be considered sustainable. The Ministry of the Environment released a guideline entitled "Towards Financially Sustainable Drinking-Water and Wastewater Systems" that provides principles for achieving sustainability. Listed below are nine principles developed by the Province, which York Region has included in preparing its Water Financial Plan.

1. Ongoing public engagement and transparency can build support for, and confidence in, financial plans and the system(s) to which they relate.
2. An integrated approach to planning among water, wastewater, and storm water systems is desirable given the inherent relationship among these services.
3. Revenues collected for the provision of water and wastewater services should ultimately be used to meet the needs of those services.
4. Life-cycle planning with mid-course corrections is preferable to planning over the short-term, or not planning at all.
5. An asset management plan is a key input to the development of a financial plan.
6. A sustainable level of revenue allows for reliable service that meets or exceeds environmental protection standards, while providing sufficient resources for future rehabilitation and replacement needs.
7. Ensuring users pay for the services they are provided leads to equitable outcomes and can improve conservation. In general, metering and rates can help ensure users pay for services received.
8. Financial plans are "living" documents that require continuous improvement. Comparing the accuracy of financial projections with actual results can lead to improved planning in the future.
9. Financial plans benefit from the close collaboration of various groups, including engineers, accountants, auditors, utility staff, and municipal council.

York Region's Water Financial Plan built on Ministry of the Environment guidelines for sustainability

The Water Financial Plan is built on the principles of sustainability mentioned above. The Region's water rate strategy has been derived using the following processes which correspond to the Principles identified by the Province as listed below:

- A detailed assessment of current and future capital needs including an analysis of potential funding sources (Principles 2, 4, 5, 6, 9)
- An analysis of fixed and variable operating costs to determine how the costs will be impacted by evolving infrastructure needs and system growth (Principles 2, 3, 6, 7, 9)

- Ongoing review of actual expenditures and establishment of forecasts in an effort to identify cost saving opportunities and enable enhanced planning of operating and capital expenditures (Principle 8)
- Review and recommendation(s) on rate structures that ensure revenues are equitable and sufficient to meet system needs (Principles 2, 3, 6, 7, 9)
- A process that involves consultation with stakeholders including staff, Council and local municipalities with the aim of gaining input and collaboration on the sustainability of the financial plan (Principles 1, 9)

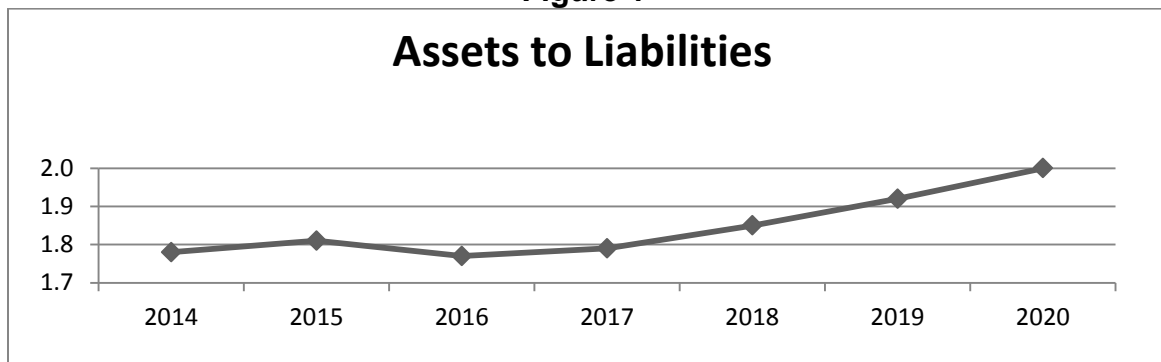
York Region's Drinking Water Financial Plan is sustainable

Good fiscal planning strives to balance revenues, expenses and asset/liability management. Main Indicators of Government Financial Condition, as outlined by the Canadian Institute of Chartered Accountants, 1997, include sustainability indicators, which focus on whether or not the Region can maintain service levels without additional debt or deterioration of the current financial position and these indicators can be used to demonstrate the sustainability of this water financial plan.¹

Assets to liabilities ratio indicates accumulated surplus through 2020

An asset to liabilities ratio indicates the extent to which operations are financed by debt. Anything above 1.00 indicates accumulated surplus. A ratio under 1.00 indicates a weak financial position to repay debt. Results for this sustainability ratio indicate an asset to liability ratio of 1.78 in 2014 with an overall increase through 2020 where the ratio is 2.00 (Figure 1).

Figure 1



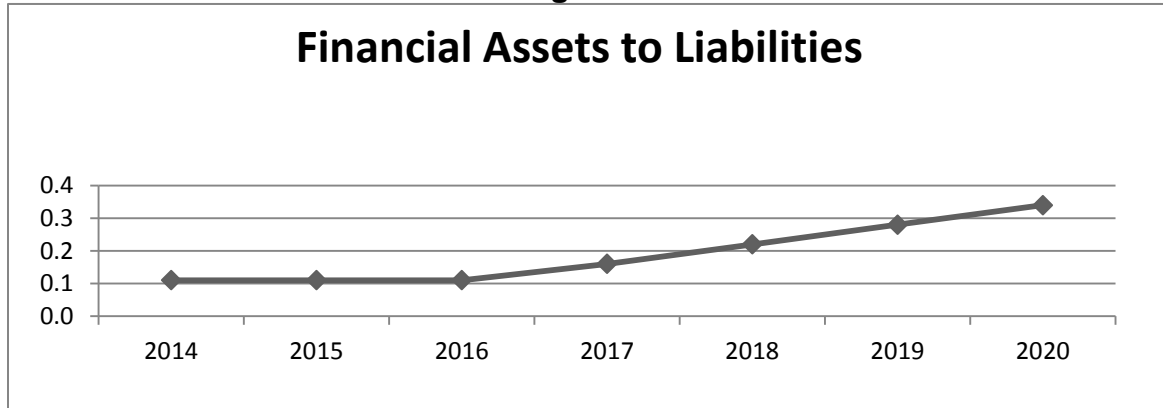
Financial assets to liabilities ratio indicates improvement through 2020

A financial assets to liabilities ratio indicates the extent to which financial assets can fund future operations. Financial assets are defined as non-tangible assets, such as cash and accounts receivable. Anything above 1.00 indicates that financial assets exceed liabilities.

¹Statement of Recommended Practices (SORP)

Due to existing high levels of debt to fund the capital plan, this ratio is not above 1.00 for the time period of this financial plan; however, it does show substantial improvement from 2014 to 2020 as the ratio increases from 0.11 in 2014 to 0.34 in 2020 (Figure 2).

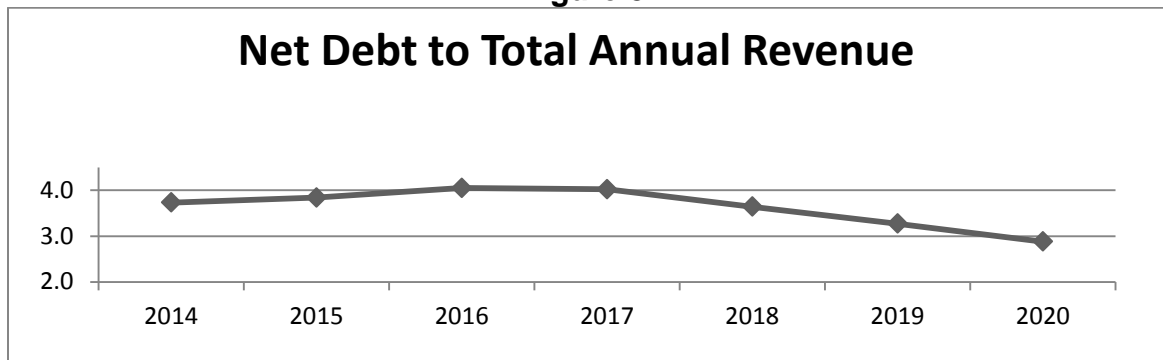
Figure 2



Net debt to total revenue ratio indicates improvement after 2017

Net debt to total revenue ratio is a measure of the amount of future revenue that is required to pay for past transactions. Net debt is calculated as total liabilities and debt less financial assets. A decreasing ratio indicates less time is needed to eliminate net debt. Although this ratio increases for the years 2015 and 2016, there is an overall decrease during the term of this financial plan with a ratio of 3.73 in 2014 decreasing to 2.88 by 2020 (Figure 3).

Figure 3



Net debt position rises from 2015 to 2017 and declines thereafter

Section 4 of *Attachment 1* contains the detailed financial plan information. Due to the level of existing debt and anticipated issuance of new debt predominantly for growth-related capital expenditures, the Region's water system will be in a net debt position of \$759 million in 2014. The Statement of Financial Position developed for the Region

forecasts an increasing net financial debt position in the 2015 to 2017 forecast period as debt levels continue to rise. However, in 2018 to 2020, the estimated net financial debt position improves each year as debt levels decrease.

Statement of operations proves to be financially viable over the long term

The Statement of Operations developed for the Region forecasts annual surpluses throughout the term of this financial plan indicating financial viability. This annual surplus is required to ensure funding is available to non-expense costs, such as tangible capital asset acquisitions, reserve/reserve fund transfers and debt principal payments. The Region also maintains an accumulated surplus throughout the period of this financial plan indicating that available net resources are sufficient to provide future water services.

Planned use of debt to construct capital and fund development charge shortfall resulting from timing

The Statement of Changes in Net Financial Assets/Debt indicates whether revenue generated was sufficient to cover operating and non-financial asset costs (i.e. inventory supplies, prepaid expenses, tangible capital assets, etc.) and in so doing, explains the difference between the annual surplus/deficit and the change in net financial assets/debt for the period. Table 4.3 of *Attachment 1* indicates that forecasted capital expenditures exceed forecasted net revenues in each year between 2014 and 2017, resulting in a decrease in net financial assets. However, in 2018 to 2020, forecasted revenues exceed forecasted expenditures resulting in an increase in net financial assets. The overall net debt position is due to the planned use of debt to construct capital assets and fund development charge timing shortfalls. Water and wastewater infrastructure is required to be built in advance of growth, with debt used as a tool to fund projects until the development charges can be recovered.

Cash position of water system indicates consistent increases through 2020

The Statement of Cash Flow summarizes how the water system is expected to generate and use cash resources during the planning period. Transactions that provide/use cash are classified as operating, capital, investing, and financial activities as shown in Table 4.4 of *Attachment 1*. This statement focuses on the cash aspect of these transactions, and thus, is the link between cash and accrual based reporting. Table 4.4 of *Attachment 1* indicates that debt, investment income and cash on hand will be used to fund tangible capital asset acquisitions over the forecast period. The financial plan anticipates the cash position of the Region's water system improving from approximately \$36.4 million at the beginning of 2014, to \$281.8 million by the end of 2020.

Significant changes from previously approved financial plan

In the previous financial plan, accounting principles required York Region to expense yearly capital investments to the City of Toronto and the Region of Peel rather than record them as assets. As a result, the Statement of Operations indicated yearly accounting deficits through 2017. Since presenting the previous financial plan, auditors have recognized the long-term benefit of cost shared capital, allowing cost shared capital with City of Toronto and Region of Peel to be recognized as a component of tangible capital assets (work in process) on the Statement of Financial Position and to be amortized over the life of the assets. This change has created a positive effect on the Statement of Operations as surpluses are now reflected over the entire period of this financial plan.

The current financial plan incorporates the Region's integrated fiscal strategy which considers project prioritization and optimizes timing of capital expenditures while maintaining desired service levels. As a result, the capital plan has been realigned since approval of the previous financial plan, resulting in several projects being deferred, without compromising service levels. This realignment has resulted in reduced debt levels and payments for the time period covered by this current financial plan improving the Region's financial position and ensuring the long-term sustainability of York Region's water operations.

Link to key Council-approved plans

York Region's Water Financial Plan, presented in *Attachment 1*, has been prepared drawing on financial information and details contained in the approved 2014 Operating and Capital budgets, 2014-2023 10-year Capital Plan and the 2011 Council approved rate study. The financial plan aligns with the Region's 2011 to 2015 Strategic Plan objective of managing the Region's finances prudently.

5. FINANCIAL IMPLICATIONS

There are no direct financial impacts as a result of the preparation of the Water Financial Plan. By approving the Plan, Council endorses the financial viability of the Region's drinking water system. This Financial Plan, along with the rate structure review and upcoming rate study, will be used to inform rate proposals that will be presented to Council in late 2015.

6. LOCAL MUNICIPAL IMPACT

With Council approval of the Water Financial Plan, Environmental Services staff will be in a position to submit the renewal application for York Region's Municipal Drinking Water License. Local municipalities will also be required to submit new water financial plans in accordance with the *Safe Drinking Water Act, 2002* regulations to renew their current licenses.

7. CONCLUSION

It is recommended that Council endorse the Water Financial Plan (*Attachment 1*) and authorize its submission to the Ministry of the Environment and the Ministry of Municipal Affairs and Housing as required under the *Safe Drinking Water Act, 2002* (Ontario Regulation 453/07). Once endorsed, staff will advertise the availability of the Financial Plan in local newspapers and on the Region's website.

For more information on this report, please contact Lucas Cugalj, Director of Strategy and Business Planning for Environmental Services at (905) 830-4444 Ext. 75041.

The Senior Management Group has reviewed this report.

Attachment (1)