REVISED 4.

HALIFAX
REGIONAL MUNICIPALITY

PO Box 1749
Halifax, Nova Scotia
B3J 3A5 Canada

Halifax Regional Council
May 30, 2006

TO: Mayor Kelly and Members of Halifax Regional Council

SUBMITTED BY: Geri Kaiser, Acting Chief Administrative Officer

DATE: May 30, 2006

SUBJECT: **Waste Water Funding Strategy**

ORIGIN

- In-Camera Meetings Mar.21, and Apr.4, 2006 - Stormwater and Wastewater Compliance
- April 11 & 18, 2006 Committee of the Whole - Council Focus Area: Infrastructure
- May 2, 2006 Tabling of the Capital Budget - Staff committed to present a wastewater funding strategy to Council as a separate report, prior to approval of the Operating, Capital, and Reserve budgets.

RECOMMENDATION

It is recommended that :

1. (A) Council approve the collapse and consolidation of Reserves used to support HRM's Stormwater and Wastewater Program, by amending Sewer Charges By-Law S-100 and any other relevant documents, and direct staff to return to Council with a new reserve business case.

   (B) Council direct staff to look for other opportunities to improved the Sewer Charges By-Law and make it administratively efficient and equitable for stormwater and wastewater customers in HRM.

RECOMMENDATIONS CONTINUED . . .

2. Council authorize staff to proceed to a public hearing to increase the sewer redevelopment charge to $0.80/ft^2. Should the public hearing be unsuccessful, staff will return to Council with an equivalent funding alternative.

3. Approve the use of 100% of the Halifax Regional Water Commission annual water dividend as a funding source for the Stormwater and Wastewater Program, effective fiscal year 2006/07. The dividend is estimated to be approximately $3.6 million annually.

4. Approve the use of 50% of the Gas Tax allocation for HRM's Stormwater and Wastewater Program in fiscal year 2007/08 ($5.1 million), with 08/09 and 09/10 gas tax funding for Stormwater and Wastewater to be continued at a minimum of $5.1 million per year.

5. Direct staff to prepare options to reallocate the proposed capital budget to offset the increased funding for the Stormwater Wastewater Program. Staff will develop options based on discussion at Council during budget debate, and Council will have an opportunity to approve the reallocation prior to voting on approval of the Capital budget.

6. Direct staff to prepare a report to Council to initiate the Eastern Passage Sewage Treatment Plant and increase the proposed 2006/07 Capital Budget, recognizing that in order to meet the debt payments from 2009/10 onward, there are funding alternatives to be considered, as outlined in the Discussion section of this report.

7. Given that the above are short term funding strategies, direct staff **to return to Council in 2009 with respect to increasing the wastewater rate to provide more sustainable funding levels.**

BACKGROUND

During March and April 2006, Environmental Management Services presented information to Regional Council with respect to the current status of existing stormwater and wastewater infrastructure, including funding requirements. Priority 1 and Priority 2 compliance related projects were described, the estimated costs of the projects, and the consequences of the work not being carried out. The Stormwater and Wastewater program is not currently financially sustainable, because revenues are declining, operating expenditures are increasing through inflation, reserve balances are declining, the infrastructure is aging, and the amount of money available for repair and rehabilitation is insufficient. With no corrective action, the Eastern Passage Water Pollution Control Plant will not be able to go forward, **many existing legal/liability and non-compliance problems will go unresolved, and new non-compliance problems** will increase.

HRM's approach to the stormwater and wastewater program has been that the beneficiaries of the system (the users) should bear the cost of the system. For this reason, the program is not funded through the general rate, as a significant portion of HRM businesses and residents do not benefit from this service. From the perspective of equity and transparency, and consistency with other jurisdictions, a rate linked to the water rate/water consumption is the best method to support delivery of stormwater and wastewater services.

Because HRM Council has expressed a desire not to increase the rate at this time, staff have analysed other funding options and have concluded that there are some short term strategies that can be put in place, but in the longer term, there will be no alternative but to re-visit the rate.

Environmental Management Services is working in cooperation with the Halifax Regional Water Commission (HRWC) to explore the potential benefits of delivering stormwater and waste water services through a utility model, perhaps as part of the HRWC. A report on the governance issues and opportunities will be presented to HRM Council on June 13th.

It is possible to develop a short term (4 year) funding strategy for stormwater and waste water, but difficult to go beyond that period because of the potential change in governance, and the potential termination of the Gas-Tax program in 2009/10.

The short term financial challenges in delivering stormwater and wastewater services are:

- The Eastern Passage project needs to go forward **as the treatment plant is out of compliance on a consistant basis, and the expansion is needed to also** enable continued development in that area, however the revenue streams are not sufficient to support debt financing the project
- The un-funded cost of dealing with Priority 1 Compliance Projects
- Building a financially sustainable program

The long term financial challenges in delivering stormwater and wastewater services are:

- The un-funded cost of dealing with Priority 2 Compliance Projects
- The extent to which the Corporate Asset Management Project will assist in infrastructure condition analysis, and capital project planning.
- Building a financially sustainable program

DISCUSSION

Reserves

Currently, the number of reserves and the rules around the use of funding in these reserves result in a situation where the by-law and funding is difficult to administer. HRM's ability to direct funding to the area of greatest need is restricted because of the rules and limitations around the use of the funds. Collapsing the reserves will require a by-law amendment process, and will require development of a new reserve business case to be approved by Council.

Q104 Sewer Redevelopment Reserve, Q105 Environmental Protection Reserve (EMS portion), Q106 Wastewater/Stormwater Management, and Q122 Water Treatment Plant Infrastructure Replacement Reserve, would be collapsed to form ideally, one reserve. **Staff had a clear sense from Council discussions during the April 11 and April 18 meetings that there was Council support for this initiative.**

Eastern Passage Water Pollution Control Plant (EP-WPCP) Expansion

Dedicating 50% of the gas tax for 2007/08, 08/09, and 09/10 to the Stormwater and Wastewater program would allow the beginning of the Eastern Passage WPCP **expansion.** This project is the largest on the immediate horizon related to Stormwater and Wastewater. The current estimate of capital cost is $30 million. The project is a Priority 1 project in that the daily flows to the plant typically exceed the rated capacity of the plant, so it is out of compliance on a consistent basis. Also, there is an expectation on the part of the regulators that HRM will be addressing this non-compliance situation in a timely manner. To that end, Council committed in principle on July 6, 2004 to provide funding to complete construction of Eastern Passage - WPCP by 2008 thereby enabling development growth to continue within the sewershed. Due to delays in necessary funding approvals even if staff's recommendations are approved today, plant construction will not likely be completed until 2009/10.

For all of these reasons, staff have looked at various options to fund Eastern Passage WPCP Expansion so that construction can be advanced as soon as possible. A portion of the project will need to be funded by debt. There are various borrowing and payback scenarios available. The project could be financed over 10 -20 years. As the gas tax funding is not secured beyond 2009/10, staff needs to develop a long term solution in order to be able to meet the debt re-payment requirements. The long term funding options include:

a) a fixed portion of the Gas Tax, if the program is continued beyond 2009/10

b) a water rate increase effective when the Harbour Solutions rate increases cease

c) increased Development Charges, Sewer Redevelopment Charges, or Capital Cost Contributions

d) realignment of HRM's capital budget. General rated funds used as debt repayment on a capital project that benefits a narrow segment of residents.

Sewer Redevelopment Charge

The Sewer Redevelopment Charge is levied on "all new buildings and all building additions in serviced areas", meaning areas that benefit from public sewer. The Sewer Redevelopment Charge was established in 1970 (36) years ago, by by-law S-100 and set at $0.30/ft^2 The charge has not changed in over 30 years. If the charge had kept pace with inflation, it would be approximately $1.63/ft^2 today. To avoid "shock" staff are not proposing a full inflation adjustment, but instead propose an increase to recover half of the effect of inflation, setting the charge at $0.80/ft^2. The increase to $0.80 per square foot would have the effect on increasing the redevelopment charge on a new 2,000 square foot home from $600 to $1,600. Currently the sewer redevelopment charge generates approximately $1.5 million in revenue annually. If the proposed increase is approved, the charge will generate an additional $2.8 million in revenue annually.

BUDGET IMPLICATIONS

In the 2006/07 Federal Budget announcement was made regarding extension of Strategic Infrastructure and Municipal Rural Infrastructure Funding. This is one example of external funding opportunities that can arise. Staff will continue to apply for these opportunities. Should we receive funding, we would include this in our overall assessment of our wastewater funding strategy.

Gas Tax
The budget implications of dedicating 50% of the Gas Tax allocation for HRM's Stormwater and Wastewater Program in fiscal year 2007/08 is $5.1 million. In 2008/09 and 2009/10 gas tax funding for Stormwater and Wastewater to be continued at a minimum of $5.1 million per year. If HRM Council approves this approach, the proposed 2006/07 Capital Budget would be modified to re-allocate funding in 2007/08 and 2008/09 from a variety of other projects, to the Stormwater and Wastewater Program.

HRWC Water Dividend
The Proposed Capital Budget would change to provide the balance of the Water Dividend to the Stormwater and Wastewater Program for for 2006/07 and 2007/08 ($2.4 million, and $1.2 million respectively). The Proposed Capital Budget already includes the full Water Dividend allocation for 2008/09.

Sewer Redevelopment Charge
The proposed increased of the Sewer Redevelopment charge would result in approximately $2.8 million in additional funding per year for Stormwater and Wastewater projects.

Capacity to Address Compliance Issues and Eastern Passage WPCP
If all of the recommendations are approved, the increased capacity to address Stormwater and Wastewater Projects is estimated to be as follows (at minimum):

Increased Funding compared to Proposed Budget	**2006/07**	**2007/08**	**2008/09**	**2009/10**
Sewer RDC	0	2,833,000	2,833,000	2,833,000
*** HRWC Div.**	2,400,000	1,200,000		
Gas Tax		5,100,000	5,100,000	5,100,000
Total New Funding	$2,400,000	$9,133,000	$11,533,000	$11,533,000

* The proposed Capital Budget includes the full Water Dividend of $3.6 million dedicated to the Stormwater and Wastewater Program starting in 2008/09.

FINANCIAL MANAGEMENT POLICIES / BUSINESS PLAN

This report complies with the Municipality's Multi-Year Financial Strategy, the approved Operating, Capital and Reserve budgets, policies and procedures regarding withdrawals from the utilization of Capital and Operating reserves, as well as any relevant legislation.

ALTERNATIVES

- Council could elect to maintain the status quo.
- Council could modify any of the recommendations above.
- Council could reject the recommendations, and request an equivalent wastewater rate increase.

ATTACHMENTS

Attachment 1 - Status quo budget, flat capital, no gas tax, HRWC dividend at $1.2 m, with Eastern Passage

Attachment 2 - Projection showing the impact if the recommendations are approved by Council.

A copy of this report can be obtained online at http://www.halifax.ca/council/agendasc/cagenda.html then choose the appropriate meeting date, or by contacting the Office of the Municipal Clerk at 490-4210, or Fax 490-4208.

Report Prepared by: Cathie O'Toole, CGA A/Director of Finance

Financial Review: Ferdinand Makani, CMA Financial Consultant

Report Approved by:
Brad Anguish, P.Eng, MBA Director of Environmental Management Services

Cathie O'Toole, CGA A/Director of Finance

Attachment One

Status Quo with Eastern Passage Sewage Treatment Plant
(no rate changes and no Gas Tax)

	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011	2011-2012
Existing Balance	**5,819,000**	**2,479,000**	**-2,851,000**	**-5,990,000**	**-12,902,000**	**-16,855,000**
WW/EPC Revenues	19,322,000	19,479,000	20,073,000	19,884,000	19,697,000	19,511,000
Sewer Redevelopment	1,700,000	1,700,000	1,700,000	1,700,000	1,700,000	1,700,000
HRWC Dividend	1,200,000	2,400,000	3,600,000	3,600,000	3,600,000	3,600,000
Gas Tax	0	0	0	0	0	0
Other	1,408,000	749,000	732,000	266,000	240,000	173,000
Total Revenues	**23,630,000**	**24,328,000**	**26,105,000**	**25,450,000**	**25,237,000**	**24,984,000**
Operating Expenditures	19,610,000	20,123,000	19,844,000	20,372,000	20,972,000	21,552,000
Eastern Passage STP	2,500,000	5,000,000	3,800,000	6,390,000	2,618,000	2,516,000
Capital	4,860,000	4,535,000	5,600,000	5,600,000	5,600,000	5,600,000
Total Expenditures	**26,970,000**	**29,658,000**	**29,244,000**	**32,362,000**	**29,190,000**	**29,668,000**
Net Gain/(Loss)	-3,340,000	-5,330,000	-3,139,000	-6,912,000	-3,953,000	-4,684,000
Closing Balance	**2,479,000**	**-2,851,000**	**-5,990,000**	**-12,902,000**	**-16,855,000**	**-21,539,000**

Notes:

Existing WW/EPC revenues decline as water consumption continues to decline. New customers are built into the revenue forecast. Sewer Redevelopment is also expected to declines but cannot be forecasted at this time.

Operating Expenses are assumed to increase 3% per year.

The gas tax agreement expires in 2009-2010.

The water dividend is fully phased in by 2008-2009.

Capital is maintained flat from the third year of the capital plan onwards, not allowing for any inflationary increases or dealing with the backlog of infrastructure deficiencies.

The Reserve Balances are in continuous decline and cannot support the Eastern Passage Sewage Treatment Plant.

Attachment Two

Eastern Passage Sewage Treatment Plant

(with Sewer Redevelopment Increase to 80 cents and $5.1m Gas Tax)

	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011	2011-2012
Existing Balance	**5,819,000**	**4,679,000**	**5,066,000**	**5,441,000**	**3,142,000**	**-212,000**
WW/EPC Revenues	19,322,000	19,479,000	20,073,000	19,884,000	19,697,000	19,511,000
Sewer Redevelopment	1,700,000	4,533,000	4,533,000	4,533,000	4,533,000	4,533,000
HRWC Dividend	3,600,000	3,600,000	3,600,000	3,600,000	3,600,000	3,600,000
Gas Tax	0	5,100,000	5,100,000	5,100,000	0	0
Other	1,408,000	734,000	753,000	272,000	69,000	0
Total Revenues	**26,030,000**	**33,446,000**	**34,059,000**	**33,389,000**	**27,899,000**	**27,644,000**
Operating Expenditures	19,810,000	20,524,000	20,444,000	21,172,000	21,971,000	22,551,000
Eastern Passage STP	2,500,000	6,000,000	5,640,000	6,916,000	1,682,000	1,616,000
Capital	4,860,000	6,535,000	7,600,000	7,600,000	7,600,000	7,600,000
Total Expenditures	**27,170,000**	**33,059,000**	**33,684,000**	**35,688,000**	**31,253,000**	**31,767,000**
Net Gain/(Loss)	-1,140,000	387,000	375,000	-2,299,000	-3,354,000	-4,123,000
Closing Balance	**4,679,000**	**5,066,000**	**5,441,000**	**3,142,000**	**-212,000**	**-4,335,000**

Notes:

Existing WW/EPC revenues decline as water consumption continues to decline. New customers are built into the revenue forecast. Sewer Redevelopment is also expected to declines but cannot be forecasted at this time.

Operating Expenses are assumed to increase 3% per year.

The gas tax agreement expires in 2009-2010.

The water dividend is fully phased in by 2008-2009.

Capital is increased in 2007-2008 and 2008-2009 and then maintained flat, not allowing for any inflationary increases or dealing with the backlog of infrastructure deficiencies. Additional operating is included for the larger number of capital projects.

The Reserve Balances are stable until 2009 and than start to decline. At this point they can longer support even a modest HRM capital program and the Eastern Passage Sewage Treatment Plant.