

# Admin Report - Asset Management Plan for Saskatoon Light and Power.docx

## ISSUE

This report and its attachments provide updated information on the asset management funding plan for Saskatoon Light & Power (SL&P).

## BACKGROUND

An asset management plan for SL&P was received as information at the Standing Policy Committee on Environment, Utilities and Corporate Services at its meeting held on March 12, 2018.

At that time, it was indicated that there was a \$7 million annual funding gap between the existing funding provided for capital rehabilitation and the required capital investment. A funding increase from \$16.1 million to \$23.1 million per year would be required to achieve the desired condition targets.

A potential funding plan was identified with the goal of bridging the funding gap to enable the assets to reach the desired condition. The foundation for the plan was to maintain the utility's existing return on investment (ROI) at the current level while directing any additional funds that may result from future rate increases directly to growing the capital provision. Based on a number of assumptions, it was projected that the funding gap would be eliminated in 2023 and ROI could again increase. This funding plan would have no direct impact on the property tax. The plan also envisioned that grants-in-lieu would continue to grow as a result of rate increases and would provide increasing financial benefits to reduce pressure on property taxes in future years.

The original asset management plan submitted in March 2018, is provided for reference (Appendix 1). The potential plan to address the funding gap is outlined on pages 12 to 14.

This report provides updated rate increase information; assumptions for future projections; and three funding scenarios for future consideration.

## CURRENT STATUS

One of the key assumptions in the funding plan was that retail electricity rates would increase 5% annually from 2018 to 2020, and then 3% thereafter. This assumption was based on the best information made available at the time from SaskPower. While SaskPower provides high-level trend forecasts to its customers, detailed rate increases happen on an as-needed basis and are based on cost of servicing calculations. The rates must also go through the Saskatchewan Rate Review Panel and are ultimately approved by the provincial government.

Another key assumption is that bulk power rates paid by SL&P to SaskPower would increase at the same rate as retail electricity rates. When this happens, it provides an opportunity for SL&P to increase funding for capital improvements to our distribution

system. SaskPower had indicated that this would likely be the case for future rate increases.

Recent rate increases:

- March 1, 2018 – SaskPower introduced a 3.5% rate increase that applied both to retail electricity rates as well as bulk power rates. This was lower than the 5% rate increase anticipated.
- Fall 2018 – SaskPower announced that it would not be seeking a rate increase during the 2019-2020 fiscal year, which runs from April 2019 until March 2020.
- April 1, 2019 – SaskPower approved the federal carbon levy. This rate increase had minimal impact on SL&P's finances as it was intended to be a flow-through levy.
- June 2019 – SaskPower announced that it will not be seeking a rate increase during the 2020-2021 fiscal year, which runs from April 2020 until March 2021.

## **DISCUSSION/ANALYSIS**

The impact of a 3.5% rate increase in March 2018 followed by two years with 0% rate increases is having a significant impact on SL&P's ability to fund its asset management plan.

Provisions to capital reserves dropped from a total of \$16.1 million in 2018 to \$14.4 million in 2019. Preliminary budget numbers prepared by SL&P indicate that the capital provision in 2020 will be \$13.1 million, and in 2021 will be \$13.9 million.

The financial model used to project SL&P's ability to fund its asset management plan has been updated. It includes the 0% rate increases for this year and next year, and then projects 3% rate increases thereafter.

The model also escalates the asset management plan's target capital funding requirement based on an escalation factor of 2%. The initial target of \$23.1 million was established based on 2018 dollars.

Based on the updated information, SL&P will not be able to achieve its target funding within the next 10 years. The funding gap in 2029 would still be \$3.6 million.

Three potential funding scenarios have been identified for future consideration:

### Scenario 1 – Status Quo – ROI is Maintained and Grants-in-Lieu Continues to Increase

This scenario is the one that was originally envisioned in the asset management funding plan and described above. This allows the City to continue to benefit from grants-in-lieu increases while maintaining ROI at current levels. Based on this scenario, SL&P will not meet its target funding within the next 10 years.

### Scenario 2 – Financial Neutral Approach – ROI Decreases are Offset by Grants-in-Lieu Increases

Budgets could be prepared to reduce ROI by the amount that grants-in-lieu increases each year. The grants-in-lieu amount is determined by a formula applied to total

metered revenue. As rate increases occur, or electricity sales increase, the grants-in-lieu amount increases accordingly providing a net benefit to the City. This increase is not retained within the utility and is transferred to the City's general revenue. However, if the ROI decreases at the same rate as the grants-in-lieu increases each year, the net result would be no financial increase or decrease for the City. Lowering ROI for the utility would allow it to increase capital provisions annually. Based on this scenario, SL&P would meet its target funding by 2026.

Scenario 3 – Reducing Financial Benefit to the City in Order to Accelerate Asset Management Funding – ROI is Decreased Faster than Grants-in-Lieu Increases (Extended Phase-in to 10 years)

This scenario would extend the phase in period for achieving the funding target to 10 years. This would require an increased contribution of \$623,800 each year, funded by a reduction in ROI. The total financial benefit for the City would continue to increase over the 10 year phase in, though at a lesser benefit than under scenario 2 by approximately \$1.4 million.

Scenario 4 – Reducing Financial Benefit to the City in order to Accelerate Asset Management Funding – ROI is Decreased Faster than Grants-in-Lieu Increases (Initial Phase-in Timeline – 2023)

In order to maintain the previous plan to achieve the funding target by 2023, a net financial reduction (in the form of an ROI decrease) of approximately \$2.0 million annually would be required for 2020, 2021, 2022, and 2023. The total financial benefit to the City would decrease from \$47,054,300 in 2019 to \$42,225,300. This amount would then continue to increase in future years.

A chart is provided in Appendix 2 showing these scenarios against the target funding level.

In 2019, SL&P is forecasted to provide an ROI of \$24,659,700 and a grants-in-lieu of \$22,394,600, for a total net benefit to the City of \$47,054,300.

**NEXT STEPS**

The Asset Management Plan for Saskatoon Light & Power will be considered as part of the 2020/21 Budget Options discussion at the August GPC meeting.

SL&P will continue to explore other options for revenue and will continue to improve efficiency through continuous improvement.

**APPENDICES**

1. Saskatoon Light & Power Asset Management Plan
2. Annual Capital Provision Scenarios Compared To Required Target Funding

Report Approval

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