Town of
East Gwillimbury

Our town, Our future

ADMINISTRATION REPORT ADMIN2016-02

To:	Committee of the Whole Council
Date:	April 5, 2016
Subject:	Strategic Energy Initiatives: Hydro One
Origin:	Legal Services

RECOMMENDATIONS

1. THAT Legal Services Report ADMIN2016-02 dated April 5, 2016 regarding Strategic Energy Initiatives be received; and

2. THAT Council adopt the Resolution in Attachment 1 regarding an Equitable and Consistent Approach to Utility Ownership

3. THAT the resolution and this report be sent to the Premier, with copies to the Minister of Finance, the Minister of Energy, the Chair and CEO of Hydro One, the Association of Municipalities of Ontario (AMO), and all municipalities served by Hydro One.

PURPOSE

The report suggests that a resolution be sent to the Province, AMO, Hydro One and those municipalities served by Hydro One, asking that the province give more equitable financial treatment to municipalities served by Hydro One.

BACKGROUND

Funding inequalities between Hydro One and Municipal Electric Utilities

There is an apparent financial inequity between those municipalities (and ratepayers) that have, or once had, their own municipal electrical utilities and those municipalities (and ratepayers) that are served by Hydro One.

The assets of a municipal electrical utility (MEU), the annual dividends sent by a MEU to its municipal owner(s), and the growth in the assets over time, are funded almost entirely by the utility's ratepayers. The dividends and asset growth accrue to the municipalities, but the municipalities put almost none of their own money into the utilities.

The dividends and asset growth paid for by ratepayers in municipalities served by Hydro One go to the province even though the province does not put funds directly into the distribution services of Hydro One.

This creates two classes of municipalities and ratepayers in Ontario – those that benefit directly from the wealth created by electrical utilities, and those that don't. The inequality is not created by geography, or location, or the market. It is a consequence of provincial *policy*.

The inequity is a consequence of provincial policy

Under provincial policy, in the early decades of the 20th century, Ontario municipalities could choose to set up their own MEU or rely on the province for local distribution of electricity. This approach to electricity distribution appears to be uncommon, and maybe unique, in North America. Much of rural Ontario decided to receive service from the province; though the fact that at one time there were over 300 municipal utilities in Ontario indicates that many smaller municipalities did have their own MEU.

When the province deregulated the electricity system during 1998-2002, it was deliberate in its decision to let those municipalities that had an MEU own the assets through a municipal corporation, even though the assets had been paid for by the ratepayers, not the municipality. As illustrated in Attachment 2, this was part of the quid pro quo for the who-does-what exercise, or provincial downloading/uploading, occurring at that time – if a municipality received electricity assets it could reap the rewards. The converse was that if a municipality did not receive electricity assets, the province reaped the rewards.

On the one hand then, provincial policy was clear that electrical distribution asset wealth could be applied to municipal services. On the other hand, if in times past a municipal council had declined the choice to set up a utility, for whatever reason, the electrical distribution wealth went to the province. In both cases the wealth has been created by the ratepayer, not by the respective government.

The consequence is particularly acute in those formerly rural municipalities that are now urbanizing, such as East Gwillimbury. Examples are included in the more complete analysis in Attachment 2. When Richmond Hill sold its electricity utility in 2004, it had a population of 140,000. It received $132,000,000. These funds are being put to municipal purposes. When East Gwillimbury reaches a population of 140,000 it will receive $0 from any utility, because it never had one.

A further consequence is the imbalance in ratepayer contribution toward paying down the stranded debt of the former Ontario Hydro. This is outlined in more detail in Attachment 2.

It is suggested that the municipalities served by Hydro One should receive a portion of the proceeds from the sale of equity of Hydro One.

The province has initiated a process to sell some of the equity in Hydro One. Since the value of this equity has been created by ratepayers in those municipalities served by Hydro One, and since as noted above the province has already indicated that electrical distribution asset wealth be applied to municipal services, it is suggested that a portion of the Hydro One sale revenue be returned to the municipalities in the service area that generated the wealth. To this end a resolution is attached for distribution to the provincial government, AMO, Hydro One, and municipalities served by Hydro One.

It is suggested as well that Hydro One municipalities be permitted to invest in electrical distribution utilities

If municipalities served by Hydro One are concerned with utility rates and levels of service, or desire the opportunity to benefit from an ownership interest in the electric distribution utility serving their municipality (similar to the manner in which other municipalities benefit from their MEU's), their options are constrained. Options to advocate for efficient and effective services should be explored with other municipalities served by Hydro One. Options could include an equity investment in Hydro One.

However, for equity investment to occur the province must amend its legislation to allow Hydro One municipalities to invest in electricity assets. Any municipality should be permitted to invest in the electric distribution utility which serves their community. The proposed resolution requests that the province enable this.

NEED FOR PUBLIC CONSULTATION

There is no requirement for the Town to seek public consultation. However, any of the initiatives described in this report should be made available to the public for review and comment.

FINANCIAL IMPLICATIONS

There are no financial implications to beginning the dialogue initiated by the resolution attached to this report. The financial implications of a positive response could be significant.

ALIGNMENT WITH STRATEGIC PLAN

The recommendations of this report align with the following Strategic Pillar(s):

#1 Providing quality, affordable programs and services for a safe, accessible and livable community

#2 Building a complete community that provides healthy places to live, work, play and learn

CONCLUSION

This report has reviewed some of the issues in respect of the inequities in Ontario's current electricity revenue system as it relates to municipalities in the province and suggests two ways to address this inequity:

1) through participation in Hydro One dividend revenue and the revenues generated by the sale by the province of equity in Hydro One, and;

2) by exploring options of working with other municipalities served by Hydro One to advocate for the efficient and effective delivery of electricity to its customers. Such options to include the investment (debt/equity) in Hydro One.

Each of the above actions will require provincial support and approval to fully implement, and it is recommended that a dialogue be commenced with the province to review and address these matters.

Prepared & Recommended by:

Original Signed By

Don Sinclair
Town Solicitor, Legal Services

Approved for Submission by:

Original Signed By

Thomas R. Webster
Chief Administrative Officer

ATTACHMENT 1

EQUITABLE AND CONSISTENT APPROACH TO UTILITY OWNERSHIP

Whereas electricity is generally available across the province; and

Whereas electricity is distributed by a municipal electric utility (MEU) or Hydro One; and

Whereas all electric distribution customers across the Province have funded the maintenance, growth and development of the electric distribution system serving them, through their utility rates; and

Whereas under deregulation the province determined that the local municipality owned the MEU serving their municipality; and

Whereas ownership of an MEU conveyed significant value to the respective municipality and therefore the ratepayers in that municipality; and

Whereas only those municipalities served by a MEU benefited financially as the owner; and

Whereas those municipalities/ratepayers served by Hydro One have not received the same benefits associated with ownership equivalent to the MEU municipalities; and

Whereas all Ontarians benefit from revenues generated from Hydro One, including those with a MEU; and

Whereas the approach taken by the province has created a significant financial inequity across municipalities;

Now therefore be it resolved that the Province be requested to consult with municipalities served by Hydro One and resolve the inequity; and

Further that provincial legislation be amended to permit municipalities to invest (debt/equity) in the Electric distribution utility serving their municipality; and,

That this Resolution be sent to the Premier, with copies to the Minister of Finance, the Minister of Energy, the Chair and CEO of Hydro One, the Association of Municipalities of Ontario (AMO), and all municipalities served by Hydro One.

ATTACHMENT 2

Inequities in the Distribution of Wealth Created by Electricity Distribution in Ontario

BACKGROUND

The province established a provincial Hydro electric system in 1906 that provided generally for generation and transmission of electricity by the province and distribution of that electricity to residents and businesses through hydro utilities in local municipalities.

In rural areas local distribution was largely provided by the province through Ontario Hydro (at that time named the Hydro Electric Power Commission) rather than the local municipality, though there were many small municipalities within the rural areas that did establish their own utilities.

Over 90 years later, through 1998 - 2002, the province introduced deregulation that required municipalities that had hydro utilities to convert the municipal utilities to corporations The municipality was deemed to be the sole shareholder of that corporation and consequently the owner of the assets of the electrical utility.

When the province began to restructure the electricity system in 1998 there were over 300 municipal electrical utilities (MEU's) across Ontario.

All electric distribution customers in Ontario funded the maintenance, growth and development of their respective electric distribution utility through their electricity rates.

Notwithstanding MEU's were funded through their distribution rates, the province determined during the deregulation exercise that MEU's were owned by the local municipality. Consequently after deregulation, municipalities with an MEU were able to receive significant annual dividend revenue or sell their MEU and its assets. This decision conveyed a significant value and financial benefit to those municipalities with a MEU and the ratepayers within these municipalities.

East Gwillimbury is the only municipality in York Region that has not had its own electricity utility

When the Regional Municipality of York was created out of the former York County in 1971, eight of the nine constituent municipalities had their own electricity distribution utility. East Gwillimbury was the only municipality in York Region that did not have its own utility. East Gwillimbury, like a number of municipalities across Ontario, was served by Ontario Hydro (now Hydro One).

Since East Gwillimbury is served by Hydro One it has never received annual dividend revenue from the utility that provided its electricity, nor will East Gwillimbury benefit from the sale of the utility assets, even though those assets were funded by the electric distribution rates paid by customers in East Gwillimbury.

ISSUES

Hydro deregulation created two classes of citizens in Ontario when it comes to the sharing of net revenue from the distribution of electricity or the sale of equity or distribution assets.

One class of Ontario residents and businesses benefitted financially when the province determined that MEU's would be owned by the local municipality which they serve. In turn revenue from electricity distribution assets could flow to the municipality to provide municipal services. This class of persons consists of those who reside or own property in municipalities that own, or did own and then sold, their own municipal electrical utility.

The other class of Ontario residents and businesses consists of those served by Hydro One. Although their electric distribution rates also funded the utility providing electricity - Hydro One - deregulation did not assign similar ownership or benefit to them or the municipality within which they resided. Consequently those residents do not receive revenue from electricity distribution assets to direct towards municipal services.

Issue 1: Inequitable and Inconsistent Approach to Electric Distribution Utility Ownership

During the 1998-2002 restructuring of the electricity system the government of the day made a *policy* decision that those municipalities that had an MEU could actually own that MEU. Municipal electrical utilities certainly were operating and managing local distribution, but it is apparent that actual ownership hadn't been clear.

> Hansard records the Minister saying in the legislature (the Hon Jim Wilson, Minister of Energy, Science and Technology):
>
> > "Our legislation gave municipalities the tools they requested. The act clarified that municipalities own their electricity utilities. Local councils are the shareholders."
>
> And a commentator on energy policy in Ontario, lawyer Robert Warren, has noted:
>
> > "The reason municipalities own these corporations is that [former Ontario Premier Mike Harris] said we are going to download costs and in

> compensation we will give you a cash cow, which will generate a return for you each year."

This is absolutely not the case for those municipalities like East Gwillimbury served by Hydro One. East Gwillimbury and other municipalities served by Hydro One were left out of that equation and had no access to any such cash cow. There was no equity or offsetting compensation provided to municipalities served by Hydro One. As a result the process can be described as biased and unfair against municipalities served by Hydro One.

If the government of the day rationalized that the ratepayers in a municipality could own the electrical distribution assets in that municipality (in part presumably because their distribution rates over the years had paid for those assets), should not the same rationale be applied to the ratepayers in the municipalities served by Hydro One, whose rates have enabled Hydro One to construct and own the assets that have been built over the years? Similar to MEU's throughout the province, Hydro One's ratepayers should have access, through their municipalities, to the net revenue and the value of the assets of Hydro One.

Issue 2: Inequitable and Inconsistent Sharing of Revenue from Operations and or from the Sale of Equity and/or Assets

Those municipalities that have retained their MEU's, or have sold their MEU's, have been able to direct annual dividends, or proceeds from sale of the utility, to municipal services for their residents and businesses and to off-set provincial downloading.

The annual dividends of Hydro One go the province. They are not returned to the municipalities/ratepayers being served by that utility.

Ironically under the current system those municipalities served by their own MEU benefit from the assets they funded and the revenue that is generated and they also indirectly benefit from the revenue generated by Hydro One through receipt of provincial services, yet they haven't contributed to the funding of the Hydro One assets that generated the revenue.

The financial benefit to non-Hydro One municipalities can be significant

The following are two examples of the financial benefit resulting from the province deciding that the local municipality owned the MEU serving their municipality;

1. When the Town of Aurora sold its electricity utility in 2006, it had a population of 38,000. It received $32,000,000. Attachment 2A shows how Aurora directed these funds.

2. When the Town of Richmond Hill sold its electricity utility in 2004, it had a population of 140,000. It received $132,000,000. Attachment 2B shows how Richmond Hill initially directed these funds.

When East Gwillimbury reaches the respective population levels noted above, it will have no such revenue or asset base whatsoever, and therefore no opportunity to direct such revenue to directly benefit its residents and taxpayers.

Issue 3: Unequal burden of paying down the stranded debt of Ontario Hydro

The net income (minus interest) of Hydro One is directed to the Ontario Electricity Financial Corporation towards retiring the debt and other liabilities of the former Ontario Hydro. The net income from MEU's is retained within the respective municipal ownership.

The debt is largely a result of construction of nuclear generation facilities that serve **all** persons and businesses in Ontario, whether through Hydro One or a local MEU.

An MEU ratepayer receives his/her dividend in municipal services. A Hydro One ratepayer, though, does not receive such a dividend. That "dividend" goes toward paying down a debt that was created to serve all Ontarians. And to the extent that the Hydro One ratepayers have contributed towards paying down the Ontario Hydro debt, the burden is lessened on the MEU ratepayers.

Issue 4: Transfer of Wealth from the Hydro One Service Area to Areas Serviced by Other Municipal Electrical Utilities

The wealth created through the service and growth of Hydro One is not generally urban (other than Brampton Hydro). It is substantially generated and created in rural Ontario.

The announced intention of the province is to use a portion of that wealth - $9,000,000,000 - to pay down provincial debt and to construct urban transit and infrastructure. This is in part a transfer of wealth created and based in rural Ontario to public services based in urban Ontario.

The intent to improve transit, to relieve congestion, facilitate movement, improve persons lives, improve competitiveness, and so on, is unassailable. To source the funds from a pool of wealth while ignoring the ratepayers who have created that wealth seems unfair. The rural source of the wealth and income is not acknowledged or respected.

Creating Equity in the Ownership of Electric Distribution Utilities

Unlike municipalities that now own their utility, municipalities served by Hydro One have little ability to impact the efficient and effective delivery of electricity services within their municipality.

If municipalities served by Hydro One are concerned with utility rates and levels of service, or desire the opportunity to benefit from an ownership interest in the electric distribution utility serving their municipality (similar to the manner in which other municipalities benefit from their MEU's), their options are constrained. Options to advocate for efficient and effective services should be explored with other municipalities served by Hydro One. Options could include an equity investment in Hydro One.

However, for equity investment to occur the province must amend its legislation to allow Hydro One municipalities to invest in electricity assets. Any municipality should be permitted to invest in the electric distribution utility which serves their community.

As a first step meetings should be coordinated with the various stakeholders including AMO, other municipalities served by Hydro One and the province. The objective of these meetings would be to gain support and develop an action plan for moving forward.

ATTACHMENT 2A

Aurora

Reserve funds established by Town of Aurora from sale of Aurora Hydro Connections Limited*

By-law 5439-12 The Aurora Hydro Sale Investment Reserve Fund

…

S.1 That the Fund be established with a balance of $31,699,391.67 which represents ninety percent (90%) of the net proceeds of the concluded sale of the Town's interest in Aurora Hydro Connections Limited.

...

S. 6 That the principle of the fund may be allocated or expended for any purpose as determined, at the sole discretion of Council, to be in the best interests of the Town …

By-law 5440-12 To Establish the Council Discretionary Reserve Fund

S.1 That the Fund be established with a balance of $3,522,155.00 which represents ten percent (10%) of the net proceeds in the concluded sale of the Town's interest in Aurora Hydro Connections Limited.

…

S.3 That the principle of the fund may be allocated or expended for any purpose as determined, at the sole discretion of Council, to be in the best interest of the Town …

*Note: although the sale occurred in 2006, these by-laws were adopted in 2012. Therefore the figures in the by-laws differ from the 2006 sale proceed because of accrual of interest.

ATTACHMENT 2B

Richmond Hill

Reserve Funds established with revenue from sale of Richmond Hill Hydro

- **Capital Asset Continuity Reserve Fund ($55 million)** will provide funding for repair and replacement of infrastructure ensuring existing capital facilities and structure are in full service and in safe operating condition
- **Community Enhancement and Economic Vitality Reserve Fund ($40 million)** for capital projects within Richmond Hill that enhance the quality of life and/or enrich the economic vitality of the community
- **Transportation Network Repair and Replacement Reserve Fund ($25 million)** will finance maintenance repair and replacement ensuring peak performance of the Town's road system network
- **Water Quality Protection Reserve Fund ($15 million)** will fund projects that protect downstream water quality and drinking water. As well, projects that rehabilitate environmental storm water systems, those that protect the Town from flooding and erosion, and those that protect downstream water courses and natural habitat will also be funded from this Reserve
- **Ecological Legacy Reserve Fund ($6 million)** will fund community based projects for the purposes of furthering ecological initiatives within the community
- **Strategic Rapid Transit Reserve Fund ($5 million)** will fund future projects that improve transportation systems in or to the Town of Richmond Hill and which are multi-jurisdictional in nature such as partnering the municipality with other levels of government and/or public/private partnerships