

# Intelligence MEMOS



From: Benjamin Dachis

To: Canadian Municipal and Provincial Governments

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Re: **TIME TO RE-THINK HOW TO DO WATER AND WASTEWATER INVESTMENT**

COVID-19 has brought forward many questions on infrastructure spending. One post-pandemic infrastructure trend comes from the likely move of many urban residents to outlying areas. House prices outside cities have risen, while condominium prices in the core [have stagnated](#). This move creates a large shift in infrastructure needs. Outlying communities will need new infrastructure, such as transit.

But transit isn't even the biggest infrastructure need. As of 2018, water and wastewater systems represent \$82 billion in asset values for Ontario cities. In comparison, Ontario municipal transit assets are valued at \$30 billion and roads at \$58 billion. In 2018, Ontario cities invested a further \$3.2 billion in water and wastewater assets that year, compared to \$2.3 billion in each of transit and roadways.

To build out new water infrastructure quickly without burdening cities or homebuyers with excess debt, provinces and cities should take steps to create standalone water and wastewater utilities. Municipal governments would still maintain ownership and the ability to set rates. But, critically, these rates should have a clearer link between the consumer end price and the amortized construction cost.

Consumers pay the full cost of water assets only if municipalities charge the full cost of both annual operations and amortization in the user cost of water. End-user rates could be a combination of a fixed capacity charge along with usage fees based on volumes. These charges could vary by neighbourhood within a city based on the infrastructure needed to service homes. When customers pay the full cost, they are implicitly making the choice of consuming the economically efficient amount of water every time they turn on the tap. Charging less than the full cost results in over-consumption. Smarter water pricing would also induce utilities to reduce leaks from their system.

However, full-cost pricing is incompatible with the current system of financing capital infrastructure upfront with development charges.

A key motivation for moving to end-user payments is to address the [consistent problem](#) in both Ontario and BC that municipal governments underspend what they collect from homebuyers via developers. Developers are paying charges expecting to get water infrastructure or other services, but are not receiving them in a timely manner.

Long-term user fees would be an attractive financing vehicle for private investors to seek to provide water and wastewater infrastructure for cities. This would free cities from financing water infrastructure with new debt or through development charges. When cities collect funds upfront for new infrastructure, there is little monetary incentive for them to complete the work on a timely basis. The incentive to expedite development of water infrastructure would be stronger if utilities had access only to water-user revenues and not taxpayer or development-charge dollars. If water utilities started receiving full payment only upon capital infrastructure completion and when users benefit from these assets, the utilities would be more motivated to provide the necessary infrastructure in a timely manner.

Another major impediment to reform is that in many municipalities water is a line-item operation within the city, indistinguishable from other city services. In contrast, a standalone water utility would be able to issue debt in its own name without recourse to taxpayers. This would lighten the upfront charge on current homebuyers, with water users paying off the debt as they used the service.

Some cities, such as Windsor (EnWin), Edmonton (Epcor) or Innisfil (InnServices) in Ontario's Simcoe County, have moved their water services into separate corporations. These municipalities have also taken steps toward integration with local electricity companies to take advantage of economies of scope in similar types of billing or administrative services. Separate utilities would also be better positioned for future mergers or cross-border agreements to seek economies of scale.

Municipal ownership would remain. Indeed, this would be a logical extension of the current model that many cities currently pursue of contracting the operation of existing water services to utility companies. As one example, the Municipality of Brockton – which includes Walkerton, Ontario – has [contracted](#) Veolia Water Canada water services.

Water infrastructure to finance new housing development is one of the major potential areas of revenue-generating investment in post-pandemic Canada. Cities should seek out opportunities to rely on end-user pricing for water. They may want to seek the expertise of organizations such as the Canada Infrastructure Bank in assessing the potential for such a change. Cities and provinces should take the steps needed to change the pricing and governance model of water and wastewater services. The result will be more options and lower home costs along with environmental benefits of less water wastage.

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