

Making Bail

Helping Canada's water utilities out of a bad spot. BY ELIZABETH BRUBAKER

CANADA'S MUNICIPAL UTILITIES are in trouble, and it seems increasingly unlikely that the provinces will bail them out. Federal aid seems equally unlikely, given the finance minister's warnings that there will be no major new spending initiatives in the 2010 budget. But our utilities need not despair. Although public money may be scarce, private investment and pricing reforms can provide sustainable solutions to the problems they face.

Municipal residential drinking water systems face a number of challenges. Ontario's Chief Drinking Water Inspector John Stager reports that 199 systems exceeded provincial limits for total coliforms or E.coli at least once during the 2007-08 year, and 94 did so on multiple occasions. As well, 83 systems exceeded provincial limits for

lead, trihalomethanes, nitrates, or other chemicals at least once, and 67 did so on multiple occasions.

Stager also reports that Ontario Ministry of Environment inspectors found areas of non-compliance at 348 systems during the reporting year. They observed problems with the sizing, installation, and operation of equipment; they detected inadequate sampling and reporting; they identified problems with operations and maintenance manuals; and they found unacceptable flow rates.

For these or other reasons, consumers do not trust the water coming out of their taps. In March 2009, Ipsos Reid probed consumer confidence in the safety and quality of Canada's drinking water. Just 20 per cent of the Ontarians polled were very confident, while another 57 per cent

were somewhat confident. The pollster also asked consumers about the source of the water they typically drink at home, and only 34 per cent of Ontarians replied that they drink water directly from the tap. The majority (63 per cent) filter their water or drink bottled water.

Meeting provincial and consumer water quality expectations is by no means the only challenge for water providers. The Residential and Civil Construction Alliance of Ontario estimates that the province is losing at least 327 million cubic metres of treated water a year. These losses cost ratepayers an estimated \$700 million annually.

Wastewater systems are also in disrepair. In 2008, 102 sewage facilities violated provincial standards or their certificates of approval. Some of









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Canada's biggest cities—Toronto, Ottawa, Hamilton, London—failed to comply with the rules. And some communities failed again and again. Brockville had 19 exceedances, Sarnia had 23, and Waterloo had 17. Under the Canada-wide Strategy for the Management of Municipal Wastewater Effluent approved by the Canadian Council of Ministers of the Environment last February, poorly performing wastewater utilities will soon face new regulatory requirements.

Fixing these and other problems will cost billions, as will expanding the systems to meet new demand. Even if billions were available in the form of provincial and/or federal grants, municipalities would be wise to forgo them. Grants and other subsidies create perverse incentives. According to the Ontario Water Works Association and the Ontario Municipal Water Association, subsidies are counter-productive, rewarding those who neglect their infrastructure and punishing those who operate effectively.

They also cause delays—municipalities put off making essential improvements, hoping that free money might someday flow in to pay for them. When and if the free money does come, it encourages overbuilding. Grants have resulted in serious overcapacity. In 1996, 44 per cent of the capacity in place was excess to Ontario's needs. That represented more than \$25 billion in premature—in some cases, unnecessary—spending. It also gave many municipalities systems that were needlessly costly to run.

Grants also allow municipalities to under-price water. Cheap water deprives consumers of the incentives they need to conserve. It encourages waste and requires unnecessary capacity.

Private capital offers municipalities an attractive alternative to grants. Increasingly, investors such as the Canada Pension Plan and the Ontario Teachers' Pension Plan want to put their money into water utilities, which offer steady, predictable, reliable revenue streams. According to Mira Shenker, editor of ReNew Canada magazine, "This is a sector that's about to explode onto

the marketplace."

Additionally, private dollars free up public funds for other purposes and transfer financial risks. And private money tends to be used efficiently—it comes with its own due diligence, enabling municipalities to get more for less.

Despite considerable theoretical support for private investment, and years of promotion by government agencies and consultants, Canada's water and wastewater utilities have little experience with private capital. For a better idea of the possible extent of private investment, we can look to England and Wales, which privatized their water and wastewater systems in 1989. Since then, the private owners have invested about £3 billion (over C\$5 billion) a year.

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Private investment is not a magic wand. The investment will have to be recovered, and water rates across Canada are notoriously low—some of the lowest in the developed world. Low rates starve municipalities of capital and operating funds. Ontario alone has an unpaid bill of \$11 billion in upkeep and repairs. In 2003, water revenues met just 64 per cent of the costs of providing services.

For these reasons, at least seven provincial bodies have advocated pricing reforms since the early 1990s. The Water Strategy Expert Panel concluded that "consumers should pay the full cost of the services they consume," and the Environmental Commissioner of Ontario advocates full-cost recovery because it will enable systems to achieve financial sustainability and self-sufficiency, and it will encourage water conservation.

Businesspeople are also supporting pricing reforms. Last year, the CD Howe Institute released a commentary by economist Steven Renzetti, who recommended universal metering, full-cost accounting, and seasonal pricing to reflect marginal costs. Shortly afterwards, Compas polled CEOs and

business leaders for their responses to Renzetti's proposals. It reported that "immense majorities back universal use of water meters, full-cost accounting, and adequate revenue to allow full updating of equipment and processes."

Environmentalists also support full-cost pricing. In August, a coalition that included Ecojustice, Environmental Defence, Great Lakes United, and the Canadian Environmental Law Association issued a report urging the province to mandate meters and to encourage volume-based, full-cost pricing. The full-cost analysis, it added, should include source protection and water conservation.

Even consumers support higher prices. Nanos Research polled Ontarians on the issue last spring, asking them how willing they would be to pay more for water if it improved the supply of clean water for Canadians and the environment. Nearly half (47 per cent) of the respondents were very or somewhat willing to pay more for water. Only 22 per cent were somewhat or very unwilling to pay more.

Despite this extraordinarily broad support, the provinces have waffled on pricing. In Ontario, the *Sustainable Water and Sewage Systems Act, 2002*, mandating provincially approved cost-recovery plans, has never been proclaimed. The more recent Financial Plans Regulation is but a weak substitute that, according to Environmental Commissioner Gord Miller, "is unlikely to push most municipal systems towards achieving financial sustainability."

There is reason for optimism. In their recent paper on safeguarding Ontario's water resources, the Ministers of Environment and Natural Resources noted strong stakeholder support for metering and conservation-based pricing. In listing possible actions for their water strategy, they included requiring municipalities to have a pricing structure that charges all users the full cost of providing water and wastewater services. Full-cost pricing may at last be on its way, setting our water and wastewater utilities on the path to sustainability. *wc*

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