

Union Water Supply System Restructuring Business Case

Presentation to
Municipality of Lakeshore Council
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UNION WATER SUPPLY SYSTEM

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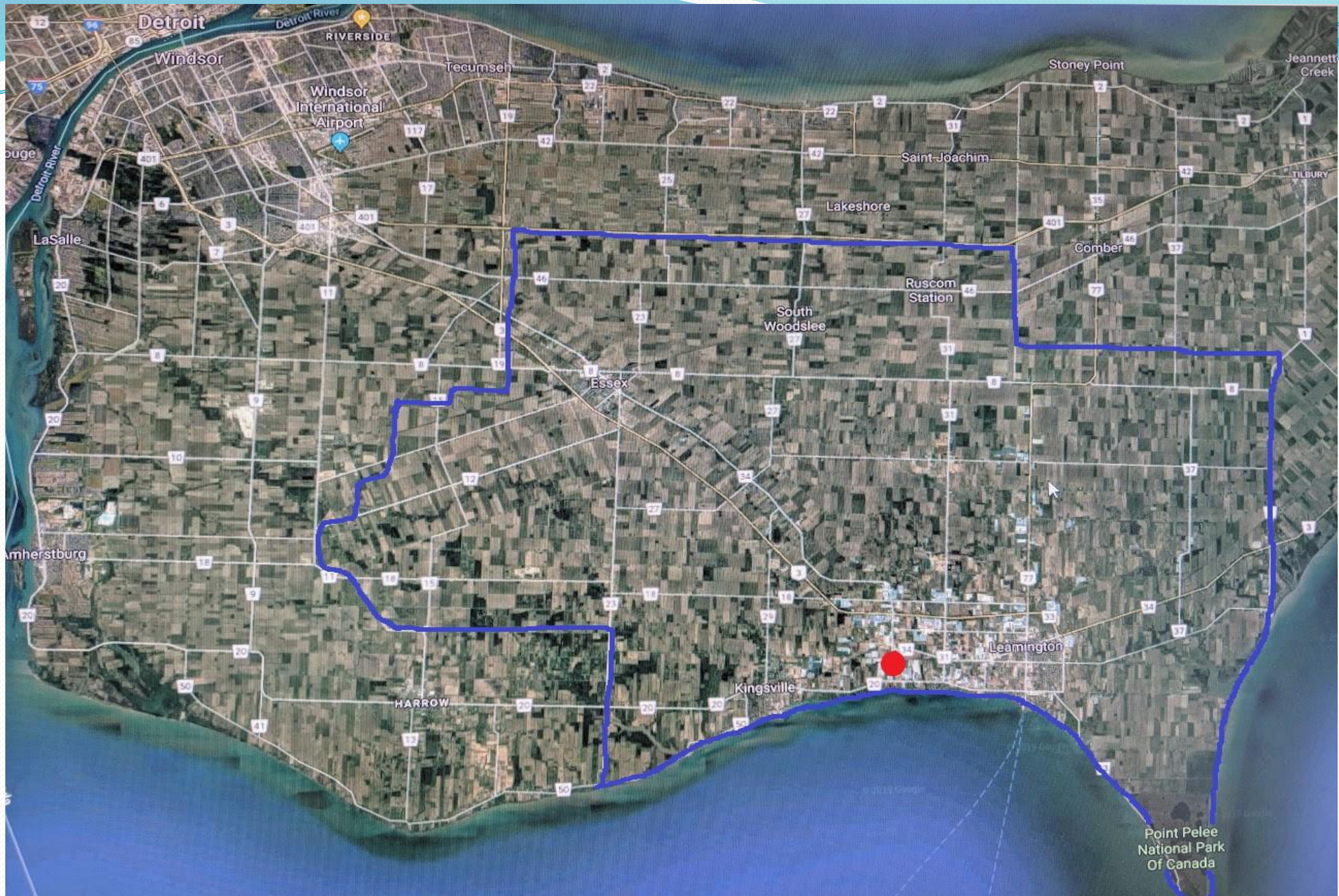


History

- The Union Water System (UWS) was commissioned in 1960 by the Ontario Water Resources Commission (OWRC).
- Original participants served by the UWS included numerous towns and townships.
- UWS facilities were owned and operated by various provincial government entities (i.e. OWRC, Ministry of Environment, Ontario Clean Water Agency) until 2001.
- As part of the *Municipal Water and Sewer Transfer Act, 1997* ownership of UWS was transferred from OCWA to newly amalgamated municipalities of Leamington, Kingsville, Essex and Lakeshore.
- The 2001 Transfer Order stipulated the creation of a Joint Board of Management that would oversee the management of the UWSS on behalf of the 4 owner municipalities

UWSS – Existing Ownership and Governance Structure

- As per Transfer Order, the interests of the Municipalities in UWSS is as tenants-in-common
- Ownership of the common system is based on each municipality's proportional consumption of the total flows of the system;
- The ownership interests were last set January 1, 2021 as:
 - Leamington – 53.00%
 - Kingsville – 38.72%
 - Essex – 4.92%
 - Lakeshore – 3.36%.
- The ownership interest is to be updated every four years.
- Board composition is based on % ownership interest as readjusted every 4 years, and currently consists of 12 appointed municipal councillors. Leamington-6; Kingsville-4; Essex-1; Lakeshore-1.



UWSS Restructuring Business Case

- UWSS to be incorporated into a Municipal Services Corporation (UWSS Inc.) under O. Reg. 599/06 of the Municipal Act
- Shareholders to consist of existing municipalities; Town of Essex, Town of Kingsville, Municipality of Lakeshore, and Municipality of Leamington.
- Initial shares to be allocated based on existing ownership (as of Jan 2021)
- Futures ownership shares to be revised every 4 years and based on water consumption;
- UWSS existing common assets to be transferred to UWSS Inc. (i.e. pumping plant, treatment plant, Cottam Booster, 4 water towers, reservoirs, common asset watermains and meter chambers)

UWSS Inc. Governance and Operation

The Governance and Operation of UWSS Inc. is established and directed through four primary documents:

- Articles of Incorporation
- Unanimous Shareholder Agreement
- UWSS Inc. General By-Law No. 1
- Water Services Agreement

Articles of Incorporation

The articles of incorporation are at the top of hierarchy of a corporation, and are the main governing documents for UWSS Inc.

- Identifies the name of the corporation and the corporate address;
- Identifies the incorporating director(s);
- Identifies the First Directors
- Identifies restrictions, if any, on business the corporation may carry on or on powers the corporation may exercise;
- Identifies the number and types of shares and the rights, privileges, restrictions and conditions (if any) attaching to each class of shares and directors authority with respect to any class of shares;

Unanimous Shareholder Agreement

The Unanimous Shareholder Agreement is an agreement between the 4 municipal shareholders that establishes the following:

- Sets out UWSS Inc.'s mandate, scope of responsibility and reporting requirements;
- Confirms that UWSS Inc. is to be internally funded (water rates, grant funding, interest income and other revenue sources), and not by way of municipal support
- Sets out Shareholder rights including but not limited to:
 - Approval of UWSS Inc. General By Law No. 1;
 - Appointment/removal of directors;
 - Approval of dividend policy;
 - the merger, amalgamation, continuance, reorganization or consolidation of UWSS Inc.
 - The issuance of new shares in UWSS Inc. or re-classification of existing shares
- Sets out which decisions require municipal approval (e.g. no core business activities, amendment to dividend policy).
- Sets out the relationship and decision-making structure between UWSS Inc. and the Shareholders; e.g UWSS Inc. employees are not shareholder employees

UWSS Inc. General By-Law No. 1

UWSS Inc. General By-Law No.1 is the primary document that directs the governance and operation of UWSS Inc. This document establishes the following:

- Sets out ownership of UWSS Inc.(Leamington, Kingsville, Essex and Lakeshore as shareholders)
- Sets of the Structure of UWSS Inc. including description of the system and assets
- Sets Board of Director composition;
- Sets out Board powers and obligations including but not limited to:
 - Appointment of Board officers and UWSS Inc. Officers;
 - Approving and controlling long-term System planning;
 - Approving and controlling System operations to meet applicable regulatory standards;
 - Approving annual operating and capital budgets;
 - Determining the annual System required revenue, and setting the associated service rates
 - Acquiring new property; or disposing of surplus property;

Water Services Agreement (WSA)

This document is an agreement between UWSS Inc. and the existing four municipalities that sets out:

- Obligations of UWSS, Inc. such as provision of water to end-users; Compensation to Municipalities for services rendered;
- Obligations of the Municipality such as Acting as Agents for UWSS Inc. for customer billing, collection and remittance of revenue; Maintenance of Distribution systems
- Revenues and rates for each municipality:
 - Underlying bulk water rate is the same for all municipalities
 - Additional sector specific rates for infrastructure improvements, bad debts, etc;
- UWSS Inc. exclusive service area
- Identifies the municipal distribution systems that are under municipal control

Other Restructuring Documents

A number of other documents have been prepared for the establishment, governance and operation of UWSS Inc. including but not limited to the following:

- UWSS Dividend Policy
- Asset Transfer Agreement
- Bill of Sale
- Real Property Transfer Agreement
- Municipal Access Agreement
- Novation Agreement – OCWA Operations and Maintenance Agreement
- Bulk Water Service Agreement
- Common Terms and Intercreditor Agreement
- Board of Directors Guidance: Reserve Accounts

UWSS Inc. Board Composition

- Board structure to consist of 12 directors to be approved by shareholders
- Each shareholder can appoint one (1) director;
- Each Shareholder can appoint an additional director for each 10% water consumption.
- For shareholders that can appoint more than 1 director, no more than 50% of director appointees (and up to a maximum of 2 total), can be either an elected official or a municipal employee. Other director appointments are to be independent of the municipality.
- Appointment of “independent” directors shall consider competencies including, but not limited to accounting, engineering, legal, and information technologies
- As a result of the above, the Board of Directors will be more independent of the Municipalities than at present

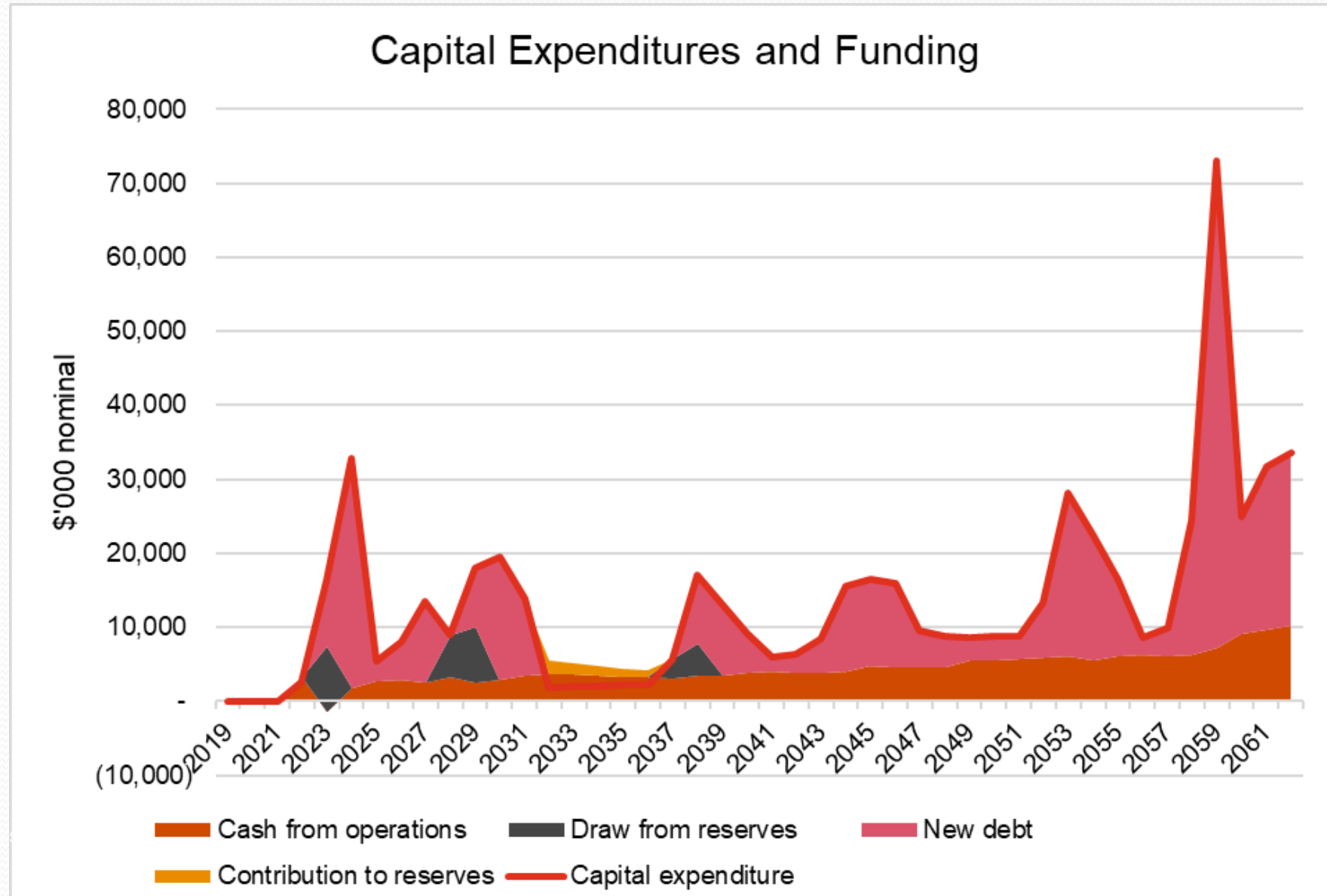
UWSS Inc. Financial Goals

- Access to grant funding at the UWSS level
- Access to debt capital at the UWSS level
- Accounting for new UWSS debt as recourse only to UWSS and not to the owner municipalities
- Ratepayer value and avoidance of “rate shock”

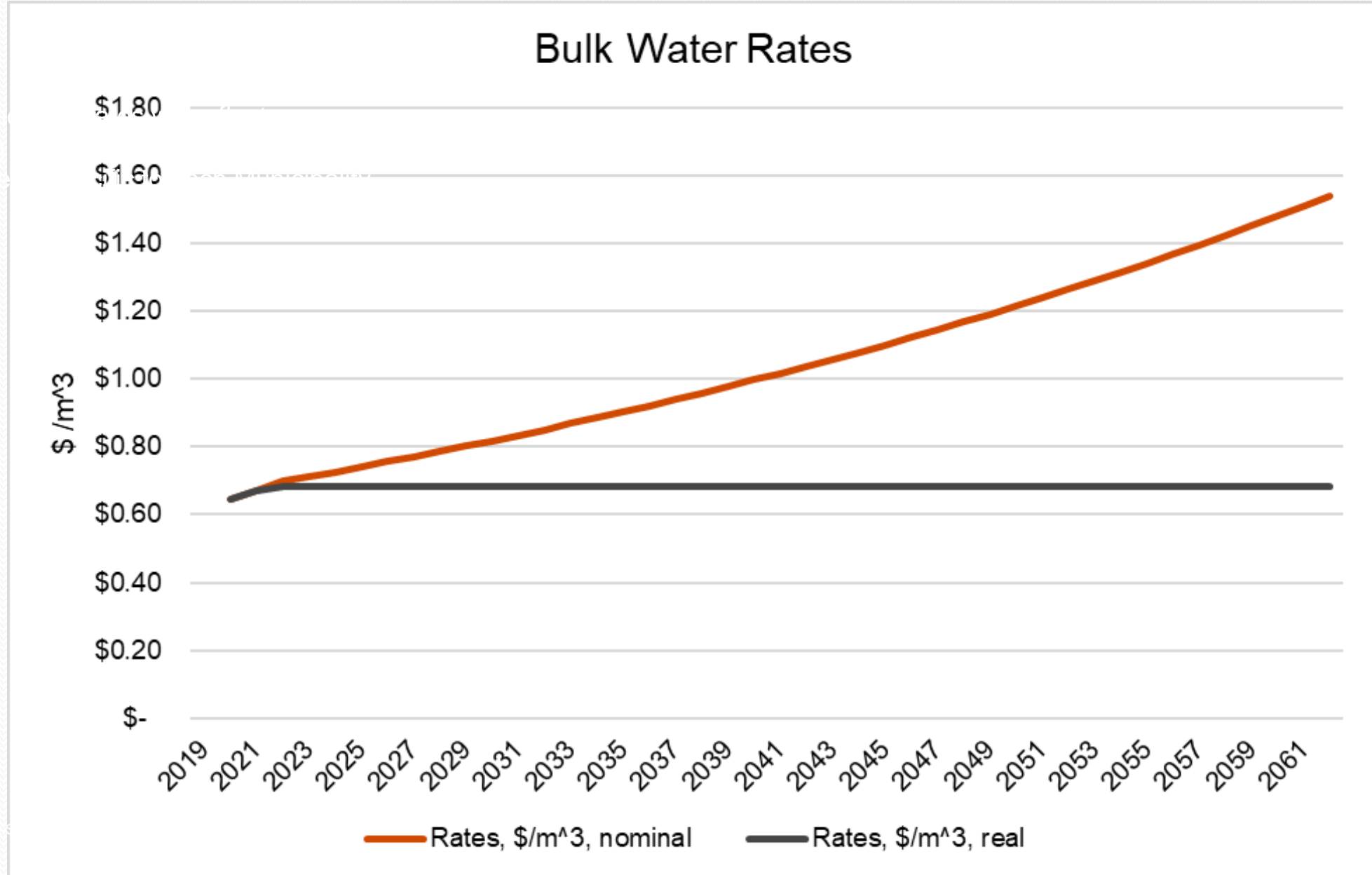
Financial Projection - Selected Assumptions

- Projection - Set out for 40+ years
- Inflation – 2% long-term
- Bulk water rates – Approved 2022 rate and 2% increase annual increase thereafter.
- Volume growth – 1.5% through 2027; 1.7% from 2028-2031; 1% thereafter
- Capital Program – Based on current 6-year capital plan (\$68 million) for 2022-2027 and includes allowance of \$48 million for works through 2031 and \$500,000 per year for unforeseen works
- Operating Costs – Based on identified operation costs through 2027 then escalated at inflation
- Grant Funding – None assumed in projection
- Existing Debt – Sun Life debt retires in 2026
- Investments – Rate Stabilization fund (\$11 million)
- Cash on hand – Based on bank account at start of 2022 (\$10 million)

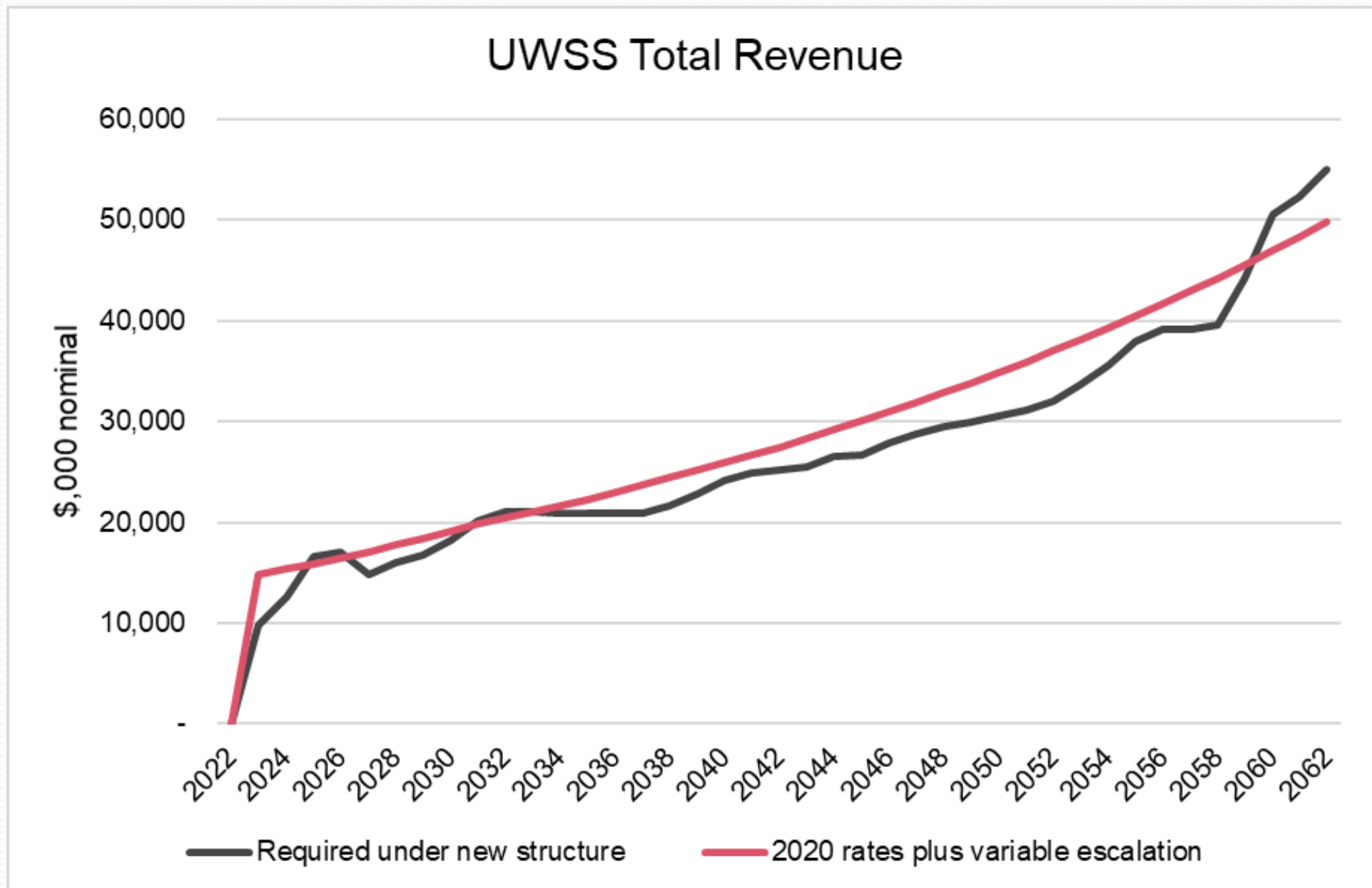
Financial Projections (1)



Financial Projections (2)



Financial Projections (3)



Summary – UWSS Restructuring

What will not change:

- Municipal ownership % interest in UWSS Inc. to continue to be based on consumption
- Sufficient capital to meet volume and quality demands
- No rate shock – uniform increases in bulk rates
- Rate structure – essentially uniform underlying bulk water rates;
- No privatization
- Cost recovery model – not a Return on Equity/shareholder profit model like electrical utilities. Any profit is re-invested into UWSS Inc.
- UWSS Inc. manages its cash reserves and investments on Board direction;
- No “Source to Tap”. Municipal distribution systems remains the responsibility of the municipalities
- OCWA contract unaffected by the new structure

What will change:

- Board of Directors will be more independent of the Municipalities than at present
- UWSS Inc. can apply for grant funding separately from the Municipalities
- UWSS Inc. can borrow on its own to finance Board-approved capital expenditures
- New UWSS Inc. debt is not attributed to the Municipalities and does not affect Municipal debt capacity
- Customers will see the UWSS Inc. portion (treatment and transmission) of their water cost separately on their bill
- UWSS Inc. will bear the initial risk of system losses, volume fluctuations and uncollectible accounts; these will be recovered in rates
- UWSS Inc. will pay a service fee to the Municipalities for work done by the Municipalities as agents of UWSS Inc.(billing, collection, and associated accounting)

Restructuring Timeline

August 2022

- Adoption of UWSS Restructuring Business Case by Councils of Essex, Kingsville, Lakeshore and Leamington

September 2020

- Incorporation of UWSS Inc. by Incorporating Director (UWSS General Manager)
- Appointment of Interim UWSS Inc. Board of Directors (Mayors of Shareholder Municipalities)
- Appointment of UWSS Inc. CEO (UWSS General Manager)
- Initial Call to Financial Institutions to Secure Financing/Funds/Credit UWSS Inc.

September-December 2022

- Establish and implement billing and revenue recovery procedures between UWSS and municipalities
- Retain new accounting/bookkeeping services for UWSS Inc.
- Establish new HR related services for UWSS Inc.
- Complete Finance Raising

Restructuring Timeline (cont'd)

October-December 2022

- Municipal selection and appointment of Board of Directors

January-February 2023

- First meeting of the Full UWSS Inc. Board of Directors
- Appointment of UWSS Inc. Board of Director Chair and Vice Chair
- Implementation of the UWSS Inc. Financial Model/Plan
- Approval of the UWSS Inc. operations and capital budgets for 2023

March-June 2023

- Initial Draw on New Financing