City of Greater Sudbury

REVIEW OF THE PROPOSED INTEGRATION OF ELECTRICITY, WATER AND WASTEWATER SERVICES

PREPARED BY

MACQUARIE NORTH AMERICA LTD

MACQUARIE

MARCH 23, 2001

Important Notice

This Report has been prepared for the City of Greater Sudbury (the "City") by Macquarie North America Ltd. ("Macquarie") in relation to the review of the proposed integration of electricity, water and wastewater services for the City.

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1. Executive Summary

1.1. Introduction

The City of Greater Sudbury ("City") has appointed Macquarie North America Ltd ("Macquarie") to review the proposed integration of electricity, water and wastewater services for the City.

The terms of reference for Macquarie require it to:

- Examine the proposed model to integrate electricity, water and wastewater services for the City;
- Assess the integrated model including its advantages and disadvantages;
- Review the cost savings that are expected to be achieved from the model; and
- Outline a plan and timetable to implement the proposed model.

In preparing this Report, Macquarie has consulted with representatives of the Greater Sudbury Utilities Inc. ("GSU" or the "Utility"), the City and the consulting firm that was involved with the development of this proposal.

1.2. Proposed Integration Model

The proposed model to integrate water and wastewater services with the electricity operations of GSU involves five core steps:

1. The City will establish a new Public Utility Commission (referred to as "Greater Sudbury PUC" or "PUC"). The establishment of a separate public utility commission is required because the *Energy Competition Act, 1998* does not allow corporations like GSU to own or lease water and wastewater infrastructure assets.

2. The City will entrust its water and wastewater infrastructure assets to Greater Sudbury PUC. This includes the infrastructure assets associated with:

   - Water treatment and distribution; and
   - Wastewater collection and treatment.

   The City and Greater Sudbury PUC would agree a mechanism for setting water and wastewater rates to be charged by the PUC. This mechanism would be designed to facilitate the transition to full cost recovery pricing for wastewater rates – water rates are presently recovering the full cost of service.

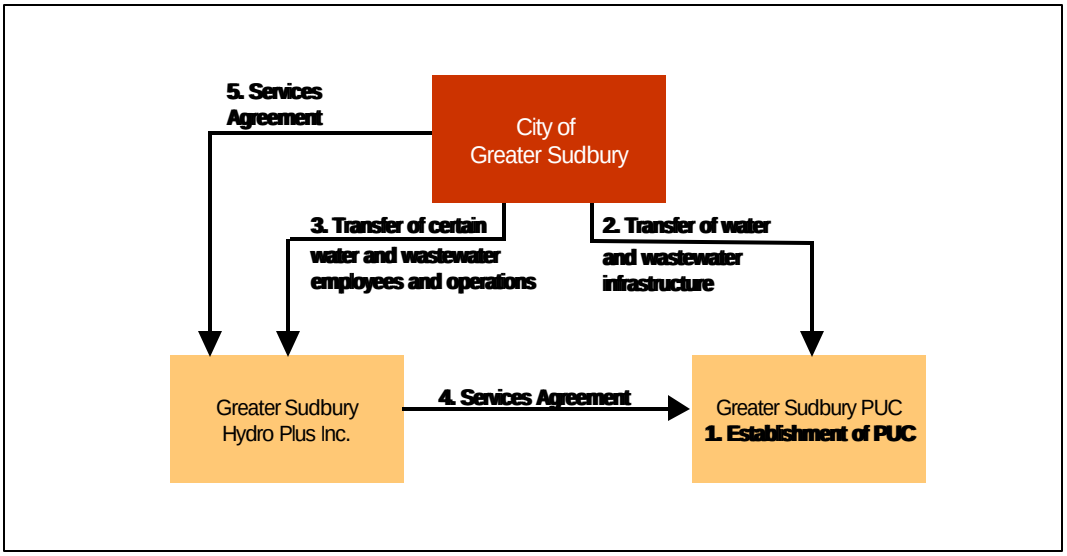
3. The City will transfer the water and wastewater employees and operations of the City related to billing and collection services and plant operations to Greater Sudbury Hydro Plus Inc. ("Servicesco"), the services company subsidiary of GSU. The City will retain employees and operations related to engineering services, including distribution and collection operations, in order to maintain synergies with the municipal roads group.

4. Servicesco will enter into a Services Agreement with Greater Sudbury PUC to operate the water and wastewater infrastructure on behalf of the PUC. This is similar to the arrangement Servicesco

has with the electricity distribution subsidiary of GSU to operate the electricity distribution infrastructure.

5. Servicesco will enter into a Services Agreement with the City to contract for the water and wastewater employees and operations retained by City.

These steps are illustrated in the following diagram.



1.3. Cost Savings

As part of the municipal amalgamation process, Utility and City staff task forces developed projections of expected cost savings. These projections estimated that cost savings of approximately $2.0 million in 2001 increasing to $3.0 million in 2003 would be available from two main sources:

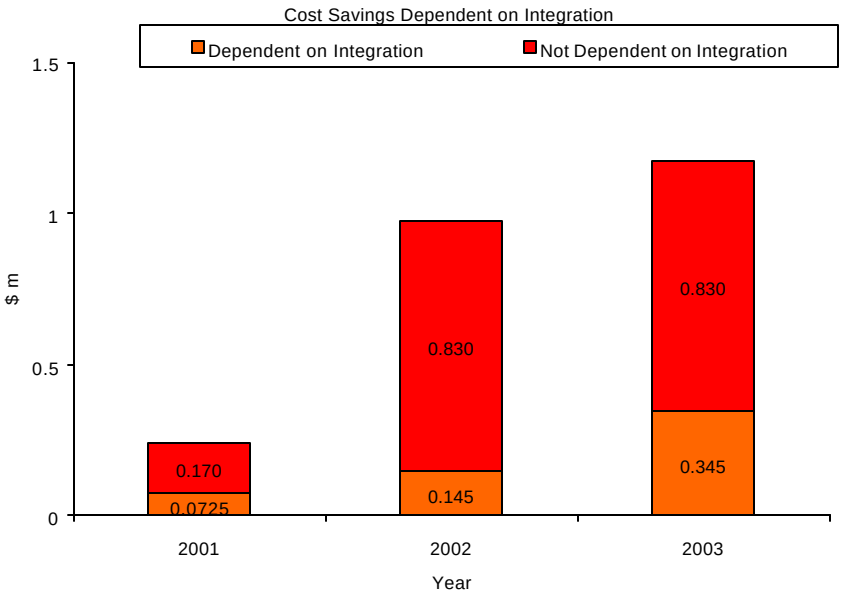
- ***Utility savings*** – savings of approximately $1.78 million in 2001 from the amalgamation and restructuring of Sudbury Hydro, Nickel Centre Hydro and Capreol Hydro to form GSU, including opportunities for synergies between the operations of GSU and those of the amalgamated municipality. These savings are projected to be achieved irrespective of whether the integrated model is adopted. Overall the Utility has been successful realising the projected cost savings from these source principally through the reduction of staff positions; and

- ***Integration savings*** – savings of $243,000 in 2001 increasing to $1.18 million in 2003 from the integration of electricity with water and wastewater services. These savings can be further divided into:

    - Savings which could only be achieved through the integrated model ($72,000 in 2001 increasing to $345,000 in 2003); and

    - Savings which could be achieved even if electricity and water and wastewater operations remained separate ($170,000 in 2001 increasing to $830,000 in 2003). For example, joint billing could be implemented without adopting the integrated model.

A review of the projected **"integration savings"** has been completed. It should be noted that because of the decision to defer the implementation of the integrated model, savings originally anticipated for 2001 have been deferred until 2002. The adjusted cost savings from integration, assuming the integrated utility model is adopted in the near future, are set out below.



Macquarie has been asked to comment on the ability to realise cost savings if the integrated model were not implemented. In this regard, we are in agreement with Navigant's assessment which stated that the City would only achieve approximately two-thirds of the identified savings if water and electricity remained separate, but it could realise all of the savings if the operations were integrated (the value of extra savings represents approximately $500,000 in savings over three years).

1.4. Model Assessment

The integration of water and wastewater services with electricity for the City provide the following benefits:

- Strategic options for costs savings and business development for GSU which enhances its financial viability and supports the City's goal of no electricity rate increases. By combining the resources into one utility, GSU will be in a better position to realize operating efficiencies and to position the Utility to earn income from providing multi-utility services to other utilities and municipalities;

- The opportunity to realise cost savings. It should be acknowledged that the majority (approximately 67%) of the cost savings identified could be realised irrespective of whether the model is adopted. The options for future cost savings not yet identified, however, are enhanced if the two organisations are integrated;

- A separate utility, rather than the municipality, providing service delivery will provide a clear mandate and commercial orientation to the provision of water and wastewater services. There was no indication that the City is not efficiently providing water and wastewater services in Greater Sudbury. One factor raised during discussion of the integrated model was the fact that development of a commercial culture was relatively new for GSU, following its recent incorporation pursuant to the *Energy Competition Act, 1998* and the introduction of performance based regulation for distribution utilities.

These advantages, however, need to be considered in light of the disadvantages. The most material disadvantage is the loss of interest income to the City if it does not retain the benefit of pre-financed capital projects. The City has a policy of pre-funding capital projects mid-year, by transferring the full capital budget allocation from the current fund to the capital fund. The lost interest income is in the order of $600,000 to $900,000 annually to the City. It should be noted that if the new Utility still has access to the

capital fund, then it would receive this interest. This additional interest would be available for the benefit of water and wastewater customers and could be used to reduce rates.

The other disadvantages – loss of representation and loss of synergies – can, on balance, be mitigated through appropriate planning, with the City and Utility working together throughout the implementation process.

There appears to be two courses of action open to the City:

- Proceed with the integration model; or
- Continue to cooperate with GSU to realise the cost savings which are not dependent upon integration (i.e., approximately 67% of the integration savings identified).

It is beyond the terms of reference of this Report to recommend either course of action to Council.

1.5. Implications for City

The City in its ten year capital plan is anticipating receiving $2.4 million (net) in interest payments from GSU in 2001. This payment was projected at the time of GSU's incorporation based on:

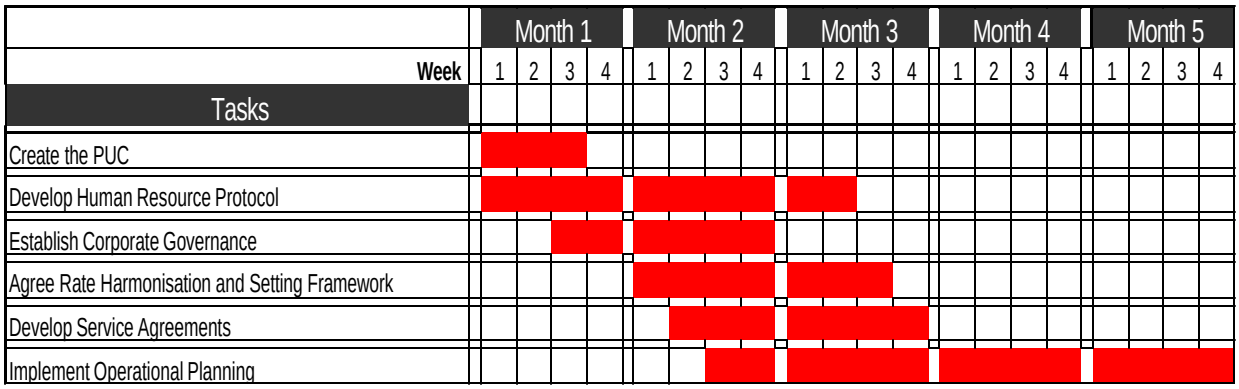
- Electricity distribution rates not being increased;
- Historic operating performance of the Utility; and
- GSU being able to reduce operating costs by $1.5 million.

The figure of $2.4 million reflects the expectation that approximately $2.8 million would be available to be paid to the City but $400,000 needs to be retained to finance growth of the telecommunication business.

With respect to the payment of the $2.4 million of interest to the City in 2001, the Utility has provided projections which indicate that after summer (when it receives a higher margin on energy sales) it will have sufficient working capital to make the interest payment to the City. The City and Utility still need to finalise the terms of the promissory note to establish the appropriate timing of payments to the City for this current year and for future years.

1.6. Implementation Plan

It is expected that the process to implement the integration of water and wastewater with electricity operations, once an in-principle decision to integrate is made by Council, could be completed over a five month period. There is a risk that this timetable could be extended to reflect the fact that both the Utility and City are still working through restructurings. A potential timetable to implement the integration with key tasks identified is set out below:


Month 1
Month 2
Month 3
Month 4
Month 5
Week
1 2 3 4 1 2 3 4 1 2 3 4 1 2 3 4 1 2 3 4
Tasks
Create the PUC
Develop Human Resource Protocol
Establish Corporate Governance
Agree Rate Harmonisation and Setting Framework
Develop Service Agreements
Implement Operational Planning

2. Background and Terms of Reference

2.1. Background

The City of Greater Sudbury was created on January 1, 2001 as a result of Bill 25, *The Fewer Municipal Politicians Act, 1999*. Seven former Area Municipalities, as well as the Regional Municipality of Sudbury, all of which were originally created under *The Regional Municipality of Sudbury Act, 1973*, were dissolved, and amalgamated under a single Municipality, the City of Greater Sudbury. In addition, unorganized territories to the south and north-east of the former Regional Municipality of Sudbury were annexed into the newly formed City.

The Province of Ontario appointed a Transition Board to direct and oversee the amalgamation and transition of all services and functions provided by the former Municipalities and unorganized territories. The Transition Board elected to consult with various groups in order to formulate its recommendations on a preferred organizational structure, staffing levels, and service delivery models for the new City.

One of the Transition Board's recommendations for the City was to integrate electricity, water and wastewater services. The proposed model to integrate these services involves the establishment of a Public Utility Commission by the new City to hold the water and wastewater assets following the City's formation on January 1, 2001. At its regular meeting of February 13, 2001, the City Council in considering this recommendation, requested additional information to be provided on the integration model. As a result, Macquarie was appointed by the City on March 4, 2001 to review the proposed integration of electricity, water and wastewater services.

2.2. Terms of Reference and Deliverable

The terms of reference and deliverables for Macquarie, as set out in the letter of engagement with the City, are as follows:

1. *Review, evaluate, and validate the findings of all reports produced by the Task Forces, Steering Committees, Working Groups, and Consultants, associated with the integration of electricity, water and wastewater services for the City.*

2. *Consult with applicable persons from the former Municipality(ies) and the Electric Utility(ies) on the operational and service level implications of implementing the proposed organizational structures at the new Utility and the City.*

3. *Explore, define, and quantify capital and operational savings that are achievable through the integration of electricity, water and wastewater services.*

4. *The Consultant will also map out an implementation time schedule in consultation with applicable City and Greater Sudbury Utilities Inc. staff.*

5. *Review and comment on the proposed model (both pros and cons).*

6. *The Consultant will provide twenty (20) copies of the final report to the City.*

7. *The Consultant will have its report ready for Friday, March 23, 2001, and present these findings to the Council of the City of Greater Sudbury on the evening of Tuesday, March 27, 2001.*

It should be noted that this Report has been prepared subject to a time constraint. Macquarie was engaged on Monday, March 4, 2001 and was required to submit a draft report by March 21, 2001, with a final report by March 23, 2001.

2.3. Sources of Information

A list of parties interviewed and information sources used by Macquarie in the preparation of this Report is attached as Appendix A.

2.4. Report Structure

This Report has been structured as follows:

SECTION	DESCRIPTION
1. Executive Summary	Presents the key findings of the Report.
2. Background and Terms of Reference	Provides the background and context for the Report.
3. Utility Services in Sudbury	Describes the utility services provided by the City and GSU in Sudbury.
4. Description of Integrated Model	Describes the proposed model to integrate electricity, water and wastewater services for the City.
5. Review of Integrated Model	Examines the advantages and disadvantages of the proposed model to integrate electricity, water and wastewater.
6. Analysis of Cost Savings	Reviews the level of cost savings expected from the integrated model.
7. Financial Implications for the City	Reviews the expected interest distribution in 2001 to the City from GSU.
8. Implementation Plan and Timetable	Provides a plan and timetable to integrate electricity, water and wastewater services for the City.

3. Utility Services in Sudbury

3.1. Introduction

This section provides an overview of the utility services provided by the City and GSU in Greater Sudbury.

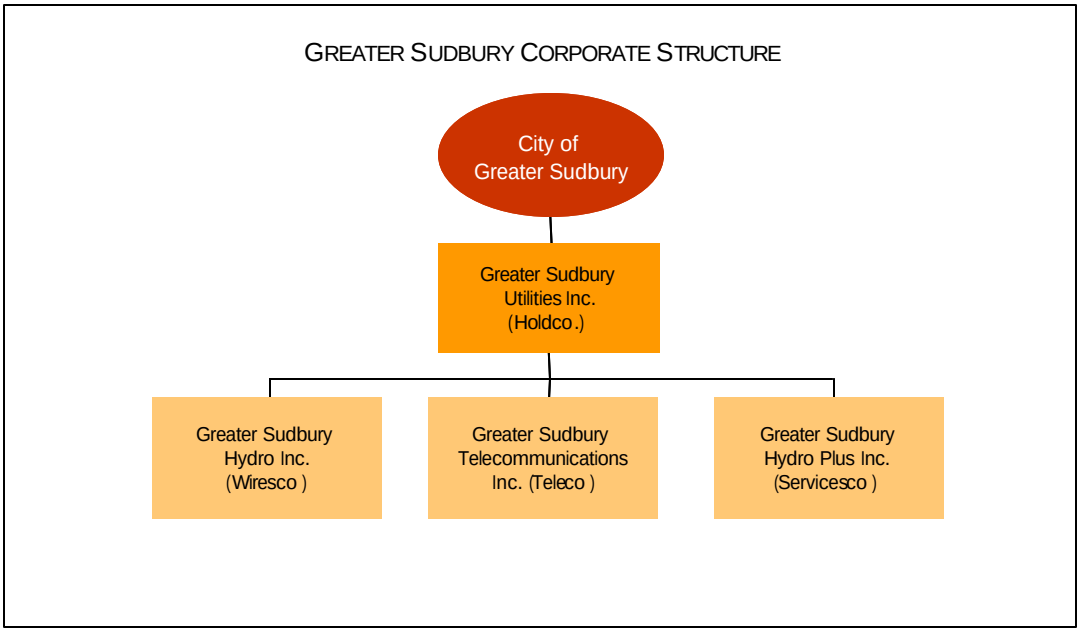
3.2. Electricity Services

The *Energy Competition Act* required each municipality throughout Ontario to incorporate their municipal electric utility under the *Business Corporations Act, Ontario* by November 7, 2000. Within the Region of Sudbury, the Transition Board had the responsibility for complying with the incorporation requirements of the *Energy Competition Act*.

The three former City utilities which the Transition Board incorporated and amalgamated to form GSU were:

- Sudbury Hydro Electric Commission ("Sudbury Hydro") which served 40,000 customers in the former City of Sudbury;
- Nickel Centre Hydro Electric Commission ("Nickel Centre Hydro") which served 1,000 customers in the municipality of Nickel Centre; and
- Capreol Hydro Electric Commission ("Capreol Hydro") which served 1,600 customers in the area Municipality of Nickel Centre.

In addition to the above utilities, Hydro One serves approximately 25,000 customers within the boundaries of the Greater City of Sudbury. GSU comprises one holding company with three operating subsidiaries. A summary of the functions of each of the successor corporations is provided below after the corporate structure diagram.



Greater Sudbury Utilities Inc. ("Holdco")

Holdco is the company which holds all the issued shares of the three other successor corporations, Greater Sudbury Hydro Inc., Greater Sudbury Telecommunications Inc. and Greater Sudbury Plus Inc. Pursuant to the transfer by-law, Holdco does not hold any other assets. The City is the sole shareholder of Holdco.

Greater Sudbury Hydro Inc. ("Wiresco")

Wiresco is the company which holds the electrical distribution assets and infrastructure and a portion of the fibre optic ring necessary for operating the electricity assets. Wiresco has three executive staff who are responsible for administering service agreements with Servicesco and managing regulatory issues with the Ontario Energy Board.

Greater Sudbury Telecommunications Inc. ("Teleco")

Teleco is the company which holds the telecommunication assets (fibre optic network and electronics) and seven employees responsible for managing the telecommunication business.

Greater Sudbury Hydro Plus Inc. ("Servicesco")

Servicesco provides utility administrative and business services to Teleco and Wiresco and hopefully in the future to other parties. As it provides utility services, it holds the majority of the employees from the predecessor hydro electric commissions and all the information technology assets (i.e. billing, accounting systems and computers etc.).

In addition to the above companies, the City is a partner with Toromont Energy in Sudbury District Energy Corporation which provides district heating, cooling and power for customers in Sudbury's downtown core.

3.3. Water and Wastewater Services

The City is responsible for the provision of water and wastewater services. Previously these services were provided by the Region of Sudbury. The water and wastewater system broadly comprises:

- 793 km of sewer mains and 10 wastewater treatment plants and associated facilities; and
- 873 km of water mains and two water treatment plants and associated facilities.

City water and wastewater services are available to approximately 95% of the geographic area of the City. In contrast, electricity services are provided by Hydro One in approximately 40% of the geographical area of the City, with the remaining 60% serviced by GSU.

3.4. Transition Board Recommendation

During the formation of the City of Greater Sudbury, the Transition Board reviewed the potential structure of utility and municipal services in Sudbury. This review involved consultation with a number of task forces comprised of Utility and municipal staff. One of the options analysed by the task forces was the integration of electricity operations with water and wastewater operations through the establishment of a separate Public Utility Commission to hold the water and wastewater infrastructure with operations being contracted to GSU.

This integrated model was reviewed for the Transition Board by a consulting team from Navigant Consulting Inc. and Miller Thomson ("Navigant"). Navigant was asked to comment on the potential advantages and disadvantages of integrating the City water/wastewater and electric utility operations. Navigant concluded, *"there was considerable merit in integrating water/wastewater and electric utility operations."* A summary of the advantages of integration identified by Navigant is attached as Appendix B to this Report.

4. Description of Integrated Model

4.1. Introduction

This section outlines the proposed model to integrate electricity, water and wastewater services for the City. As the incorporation of the three former hydro-electric commissions into GSU has been completed, the model set out below focuses upon the steps necessary to integrate these electricity operations with the water and wastewater services of the City.

4.2. Proposed Model

The proposed model to integrate water and wastewater services with the electricity operations of GSU involves five core steps:

1. The City will establish Greater Sudbury Public Utility Commission.

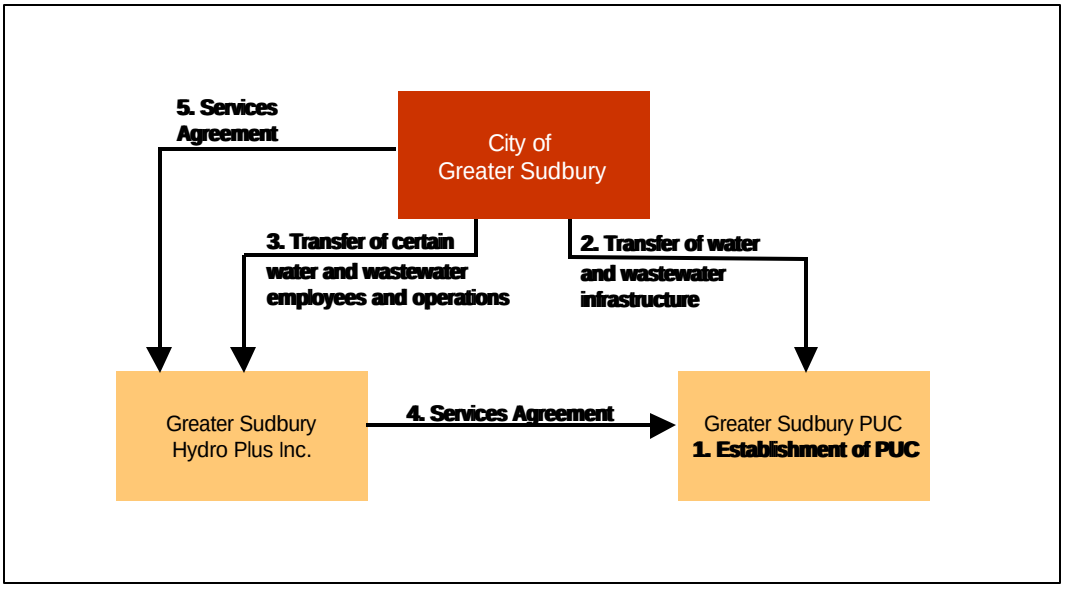
2. The City will entrust its water and wastewater infrastructure to Greater Sudbury PUC.

3. The City will transfer the water and wastewater employees and operations of the City related to billing and collection services and plant operations to Servicesco. The City will retain those employees and operations related to engineering services including distribution and collection operations.

4. Servicesco will enter into a Services Agreement with Greater Sudbury PUC to operate the water and wastewater infrastructure on behalf of the PUC.

5. Servicesco will enter into a Services Agreement with the City to contract for the water and wastewater employees and operations retained by City.

These steps are illustrated in the following diagram and are described in more detail below.



4.2.1. Establishment of Greater Sudbury PUC

The City will establish Greater Sudbury PUC by passing a by-law under the authority of the *Public Utilities Act, 1990*. A separate PUC needs to be established to hold the water and wastewater infrastructure as the *Energy Competition Act, 1998* allows corporations like GSU to manage and operate water and wastewater assets but prohibits it from owning or leasing such assets.

It was originally proposed that Greater Sudbury PUC would be governed by a commission which would consist of the Board of Directors of GSU. The rationale to have the same individuals as commissioners and directors was to ensure that there was common governance to oversee the integration of services, as well as leveraging off the commercial expertise of GSU's Board. It is understood that this feature of the proposal has been modified, at the request of City Council, such that the commission for the PUC would comprise representatives of the Board of Directors of GSU and other independent parties appointed by the City. This modification was done to ensure that there is appropriate political accountability present in the delivery of water and wastewater services.

4.2.2. Water and Wastewater Infrastructure

The City will entrust, pursuant to the by-law, its water and wastewater infrastructure to Greater Sudbury PUC. This includes the infrastructure assets associated with:

- Water treatment;
- Water distribution;
- Wastewater collection; and
- Wastewater treatment.

Greater Sudbury PUC is essentially being created as an asset owning company (like Wiresco) with the operation of the assets being contracted to Servicesco pursuant to a Services Agreement. In addition to holding these assets, Greater Sudbury PUC would adjust rates pursuant to a mechanism agreed with the City (which has the ultimate responsibility for setting water and wastewater rates). The intention with establishing the rate mechanism is to facilitate the transition to full cost recovery pricing. Transition to full cost recovery pricing is a policy objective of the Provincial Government as specified in *Operation Clean Water*, which was launched in August 2000.

Based on numbers from the year 2000, sewer rates need to be increased in the transition to full cost recovery. This is illustrated by the funding sources for water and wastewater set out in the table below.

FUNDING SOURCE	2000
Water user fees	$19.4 million
Sewer rate (25% of water rate)	$4.5 million
Sewer and water frontage charge	$0.9 million
Municipal tax levy	$10.1 million
Total	**$34.9 million**

As wastewater rates move to full cost recovery, it is expected that the contribution from the municipal tax levy will decrease proportionately.

4.2.3. Transfer of Water and Wastewater Employees and Operations

The City will transfer the water and wastewater employees and operations of the City related to billing and collection services and plant operations to Servicesco. This is expected to cover 60 employees. The key functions transferred to Servicesco relate to:

- Utility management;
- Billing and collection;
- Plant operations; and
- System control.

The water and wastewater employees and operations retained by the City relate to:

- Engineering services including distribution and collection operations; and
- Certain administration functions including human resources and payroll related to the employees retained by the City.

A key decision in the development of the integrated model was whether to transfer all City water and wastewater engineering and operations services to Servicesco. This was not favoured because it would lead to a loss of synergies presently being realised with the municipal roads group, as water and wastewater engineering and operations is performed in conjunction with road engineering by staff proficient in both areas.

The other services proposed to be retained by the City relate to certain administration functions including human resources and payroll.

In structuring the transfer of employees, it is necessary to develop a human resources protocol to deal with employee transfers. Based on legal advice, the transfer of employees to Servicesco would be a sale of a business with Servicesco being bound by the existing collective agreements.

4.2.4. Services Agreement Between Servicesco and PUC

Servicesco will have a Services Agreement with Greater Sudbury PUC to operate the water and wastewater infrastructure. This would be similar to the arrangement Servicesco already has to operate the electricity distribution infrastructure for Greater Sudbury Hydro Inc. (Wiresco).

The Service Agreements are necessary because the Affiliate Relationships Code imposes strict guidelines upon arrangements that can be entered into by electricity utilities.

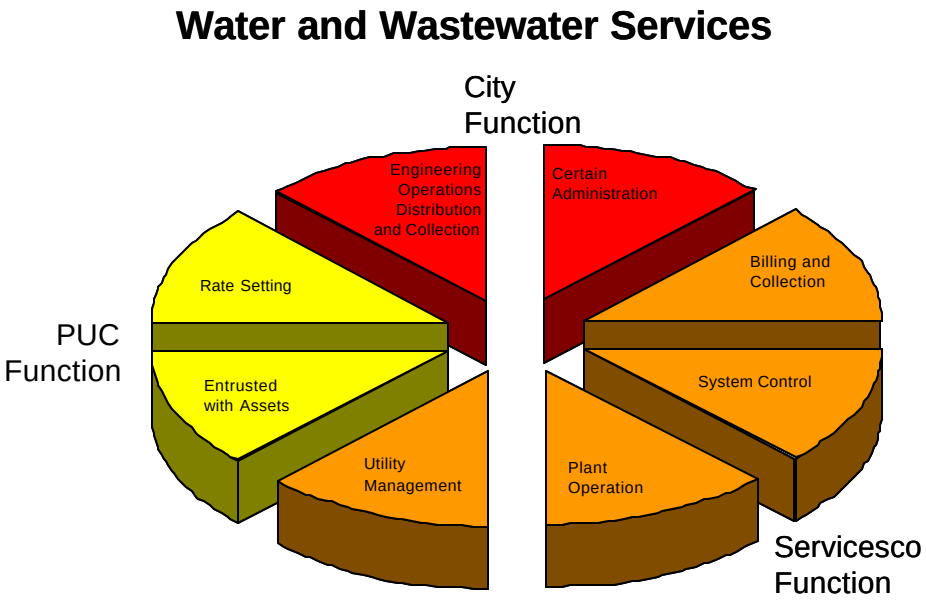
4.2.5. Services Agreement with City

Servicesco will enter into a Services Agreement with the City to contract for the employees and operations retained by the City. This applies to:

- engineering services including distribution and collection operations; and
- certain administration functions including human resources and payroll related to the employees retained by the City.

4.3. Summary of Integrated Model

Based on the model outlined above, Servicesco would be responsible for the management of the water and wastewater system on behalf of the PUC. The range of services previously carried out by the City would be divided between the City, Greater Sudbury PUC and Servicesco as set out in the pie chart below.



5. Review of Integrated Model

5.1. Introduction

This section reviews the advantages and disadvantages of the integrated model described in section 4.

5.2. Advantages of the Model

The key advantages of the integrated model include:

- Establishment of a separate service delivery utility;
- Opportunities for cost savings; and
- Development of a multi-utility services platform.

Each of these advantages is discussed below.

5.2.1. Separate Service Delivery Utility

There are a number of major challenges facing water and wastewater service delivery in Ontario including stricter standards, higher consumer expectations, capital funding shortfalls and the move to full cost recovery. The establishment of a separate PUC entrusted with the water and wastewater assets of the City, with the majority of operations being contracted to Servicesco, will have the effect of transferring service delivery responsibility to a utility, separate from the municipality. This separate utility is arguably in a better position to meet the challenges facing water and wastewater services.

The ability to meet water and wastewater challenges stems from the following features of separate utility service delivery compared to provision of the same services by a municipality:

- ***Clear mandate*** – a feature of a separate utility is that it would have a clear objective to provide water and wastewater services and be held directly accountable for the provision of those services. In contrast, if the service is provided by a municipality, it can be difficult establishing water and wastewater services as a priority given the number of services provided by the municipality.

- ***Commercial orientation*** – the governance for both Servicesco and the PUC would be run according to business principles with incentives for cost control, revenue generation and high levels of customer service. It is intended that the delivery of water and wastewater services would be able to capitalize on the commercial culture and experience of the electric utility management and Board of Directors. This will enable the business practices being applied to the electricity operations to be applied also to the water and wastewater operations.

- ***Facilitates the move to full cost recovery*** – one of the challenges facing the Ontario water and wastewater sector is the move to full cost recovery pricing. The implementation of full cost recovery is crucial to developing a long term water and wastewater investment and financing strategy. Throughout Ontario, historic investment levels have been below levels necessary to maintain and rehabilitate the system. This is relevant for the City's system, as for the year 2000 capital expenditures were approximately $10.8 million, whereas to properly maintain the system, expenditures should have been in the vicinity of $12 million to $13 million. The move to full cost recovery for water and wastewater services is a sensitive issue. Separate utilities have traditionally found it easier than municipalities to pass on cost increases to their customers. This is because a utility's charges are a proxy for the cost of delivering a service and as such should be relatively

uncontentious. A municipality, in comparison, which is funded from general taxes, typically finds tax increases a politically sensitive subject.

It is important to note that the full cost of water services is being recovered in Sudbury. It is the sewer rates which need to be increased to their full cost in any move to full cost recovery.

- ***Financial Flexibility*** – As full cost recovery prices are implemented, it should remove financial reliance upon the municipality and provide funding flexibility and independence for the water and wastewater system.

In preparing this Report, there were no indications that the City was not efficiently providing water and wastewater services in Greater Sudbury. In particular, there is nothing to suggest that the City did not have a clear mandate and the capacity to both adopt a "commercial orientation" and implement full cost recovery for the wastewater rates.

One factor raised during discussion of the integrated model was the fact that development of a commercial culture was relatively new for GSU, following its recent incorporation pursuant to the *Energy Competition Act, 1998* and the introduction of performance based regulation for distribution utilities. This factor may suggest that it may be prudent to wait until GSU has consolidated its restructuring and this commercial orientation is firmly established before proceeding with the model.

5.2.2. Cost Savings

A key rationale for integrating electricity, water and wastewater services is the opportunity to achieve cost savings. The objective is to keep these savings within the water and wastewater system by applying the savings to fund capital projects for the benefit of customers. This should, when combined with any move to full cost recovery, reduce the funding requirements from the municipal tax levy proportionality.

The savings that have been identified by the City and Utility task forces are broadly attributable to two sources:

- ***Utility Savings*** – savings from the amalgamation and restructuring of Sudbury Hydro, Nickel Centre Hydro and Capreol Hydro to form GSU, including initiatives for synergies between the operations of GSU and those of the amalgamated municipality. These savings will be achieved whether or not the integrated model is implemented; and

- ***Integration Savings*** – savings from the integration of electricity operations with water and wastewater services. These savings can be further divided into:

    - Savings which could only be achieved through the integrated model; and

    - Savings which could be achieved even if electricity and water and wastewater operations remained separate.

The cost savings identified from both "utility savings" and "integration savings" are relevant to the City because the cash flow generated is a determinant, along with the operating performance of GSU, of the expected distributions to be paid to the City. This point is discussed in detail in section 7 of this Report.

A key consideration in evaluating expected integration savings is the proportion that is dependent upon the integration of electricity, water and wastewater operations compared to those identified savings which could be achieved without implementation of the model. This consideration indicates that approximately one third of the integration savings would not be achieved if the two operations remained separate.

With respect to future cost savings initiatives, it is likely that cost savings would be easier to identify and implement as part of an operational integrated model than if the operations remained separate.

The explanation of the cost savings is discussed in detail in section 6 of this Report. For simplicity, section 6 focuses on the savings from integration as this is the focus of this Report, and "utility savings" will occur irrespective of whether the model is implemented. The "utility savings" are discussed in detail in Appendix C of this Report.

5.2.3. Development of a Multi-Utility Services Platform

The electricity industry in Ontario has undergone an unprecedented level of change over the last two years. The changes have imposed a number of challenges to the ongoing viability of utilities. For example, the introduction of performance-based regulation has imposed strict productivity improvements levels and minimum customer service standards for distribution utilities. Similar challenges are expected to be imposed on the water and wastewater industry following the Province of Ontario's *Operation Clean Water* initiative. Premier Harris has stated that the goal of *Operation Clean Water* is "to have the safest water in Canada, with high standards, frequent testing, prompt reporting and tough penalties."

The integration of water and wastewater services with electricity operations is expected to enhance the financial viability of GSU. The ability to realise cost savings from duplication in services will support the goal of no rate increases and economic development initiatives in Sudbury. In addition, the combined asset and skill bases of electricity, water and wastewater may strategically position the Utility to earn revenue from providing multi-utility services to other utilities and municipalities. For example, post-Walkerton, there is an expectation that there will be an emerging market in Ontario of municipalities looking for a professional agency – with a public interest focus – to operate water and wastewater services. Should the City be successful in acquiring the gas franchise from Union Gas, it is possible that gas could be added to this multi-utility platform.

5.3. Disadvantages of the Model

The disadvantages of the integrated model include:

- Loss of interest income for the City;
- Loss of representation for the City; and
- Loss of synergies with the City.

Each of these disadvantages is discussed below.

5.3.1. Loss of Interest Income

A major concern of the City is the potential loss of interest income from the pre-financed portion of water and capital wastewater projects. The City has a policy of pre-funding capital projects mid-year, by transferring the full capital budget allocation from the current fund to the capital fund. In turn, all interest revenue earned by the capital fund is credited to the current fund. The pre-financed portion of water and wastewater projects can range anywhere from $10 million to $15 million in any year. Using 6% as the cost of borrowing or the cost of lost interest revenue, this means a loss of about $600,000 to $900,000 in current revenue annually.

It should be noted that if the new Utility still has access to the capital fund, then it would receive this interest. This additional interest would enable it to reduce the impact on water and wastewater rates.

5.3.2. Loss of Representation

The countervailing disadvantage of creating a separate service delivery utility is a loss in representation for the local community. Even though the community, through the municipality, is the ultimate owner of the water and wastewater infrastructure, its representation and the level of political accountability at the commission level could be reduced in an effort to promote a commercial orientation.

This disadvantage has previously been raised at Utility and municipal levels in considering the appropriate governance arrangements. In particular, the original proposal to have the Board of Directors of GSU appointed as commissioners of the PUC has been modified to allow other independent parties to be appointed by the City. This modification was done to ensure that wider community interests are represented on the PUC.

5.3.3. Loss of Synergies with the City

In restructuring water and wastewater service delivery, there is a potential for duplication or an increase in costs to occur between the City's operations and those of the Utility. This duplication could result in inefficient administration and operating structures arising at either the City or the Utility.

An example of the potential loss of synergies that would occur is increased costs if there was a separation of the municipal roads group from water and wastewater engineering. This is because staff proficient in both areas performs both functions. As discussed earlier, this potential loss of synergies was identified during the development of the integrated model and the model has been adjusted to keep these staff together.

Two possible examples of loss of synergies from the model are:

- ***City administration services*** – if the Utility assumes the administration function for plant operations and billing and collection staff are transferred to Servicesco, it is possible that City may have excess capacity in its administration function; and

- ***Harmonization of Employee Costs*** - there was a concern raised that wage and benefit harmonization issues between City staff transferred to Servicesco and Utility staff could result in an increase in costs. The staff transferred to Servicesco include billing and collection and plant operations. We have been advised that wage harmonization has been factored into cost estimates for billing and collection and is not relevant for plant operations as their job descriptions are sufficiently distinct. This potential outcome will require further investigation.

6. Analysis of Cost Savings

6.1. Introduction

This section of the Report reviews the level of savings that are expected to be achieved from the integrated model. A discussion of savings expected from the amalgamation and restructuring of Sudbury Hydro, Nickel Centre Hydro and Capreol Hydro to form GSU are discussed in Appendix C of this report. This is because the utility savings are projected to be achieved irrespective of whether the integrated model is adopted.

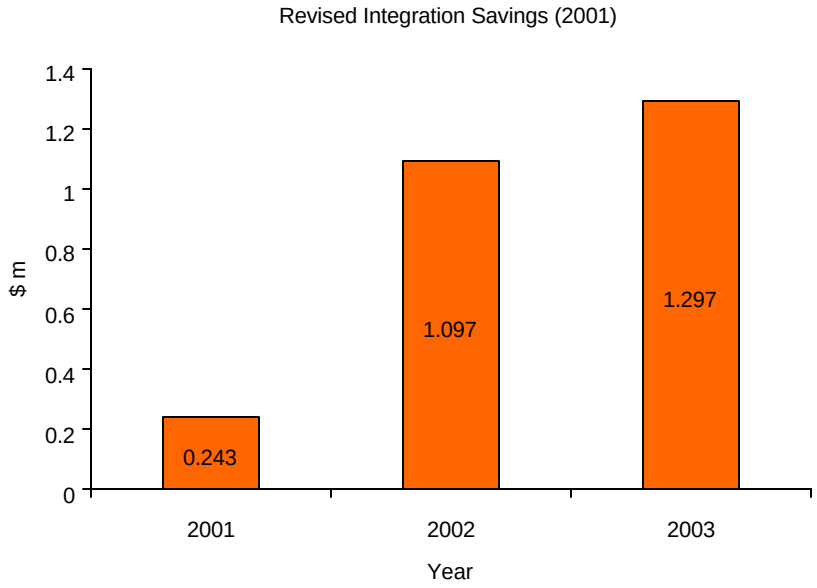
6.2. Integration Savings

6.2.1. Overview

A review of the projected "integrations savings" has been recently revised by GSU. It should be noted that because of the decision to defer the implementation of the integrated model, savings originally anticipated for 2001 have been deferred until 2002. These savings can further be divided into:

- Savings which could only be achieved through the integrated model; and
- Savings which could be achieved even if electricity and water and wastewater operations remained separate.

GSU's revised integration savings for each year are set out in the bar chart below.



The following table summarises the projected source of these savings.

$000	2001	2002	2003
Elimination of Outsourcing • Elimination of Outsourcing Arrangements	170	190	-
Elimination of Duplication • Cost Savings	73	534	200
Other Initiatives • Working Capital Improvements	-	130	-
Total Savings	**243**	**854**	**200**
Cumulative Savings	**243**	**1,097**	**1,297**

Source: Greater Sudbury Utilities Inc.

6.2.2. Elimination of Outsourcing

There are a number of services currently being outsourced by the City's water and wastewater operations to external parties which could be performed by the Utility with existing resources. This would result in cash flow, previously paid to the external parties, being paid to the Utility and being kept in the community. This is technically not cost savings but represents a better utilisation of Utility staff and maintains cash flow within the community. The identified initiatives relate to:

- Electrical Design and Supervision ($30,000 annual savings);
- Integration of Instrumentation and Control Program ($130,000 annual savings);
- SCADA Design and Maintenance ($120,000 annual savings)
- Substation Services ($80,000 annual saving)

The above cost savings represent the labour component of outsourcing arrangements. The capital cost element of these arrangements would need to be subject to a valid business case.

The City and Utility have indicated that they are willing to consider contracting services to each other on condition that:

- Any contracts do not result in an increase in costs;
- Any contracts include flexibility and performance measures such that each party is not locked into any rigid arrangements; and
- Any contracts are tested against the market to ensure that the parties are receiving best value.

Assessment:
These initiatives appear relatively straightforward and should be progressed, where practical, by the City and Utility. It should be acknowledged that all of these arrangements could be progressed without adopting the integrated model. That is, the Utility and City could progress these initiatives independent of the integration of electricity services with water and wastewater.

6.2.3. Elimination of Duplication

There are a number of cost saving initiatives identified that relate to the elimination of duplication between electricity operations and those of water and wastewater. These cost savings relate to:

- ***Water and wastewater billing*** – the Utility would provide water and wastewater billing services in addition to electricity billing. The cost savings relate to the elimination in duplications between the two billing functions at the Utility and City. Synergies in back office functions, like billing services, are being realised by many other MEUs and municipalities throughout Ontario. For example, Enwin Utilities, the services company for Enwin Powerlines (the distribution utility for the City of Windsor) provides billing services to Windsor Public Utilities Commission. The combination of water and wastewater billing services is expected to produce cost savings of $341,000 per year. One-off transition costs of $150,000 are projected to be necessary to migrate the water and wastewater customer database to GSU's system.

- ***Amalgamate meter shop*** - combine the two existing meter shops resulting in savings of $145,000 per annum but with transition costs of $20,000.

- ***Integrate control room*** - combine the water and wastewater and the electricity control rooms. Preliminary estimates for this saving are in the order of $200,000 per annum however transition costs of $200,000 are expected. Any integration of control rooms is not expected to occur until 2003.

- ***Increased plant automation*** - by automating the Wanipatae water treatment plant and the Sudbury wastewater treatment plant, it is projected that there could be a reduction in one shift per week at each plant. This would result in annual savings of $121,000 from 2002. The City has advised that this initiative is being implemented at a capital cost of approximately $600,000 in order to meet new regulations. As a consequence, this saving will be realised irrespective of any decision to pursue integration.

There are also a number of preliminary initiatives being pursued by the Utility which have not yet resulted in identified costs savings. For example, there are opportunities for the Utility to provide energy management services to the City's water and wastewater facilities.

Assessment:
The cost savings relating to the elimination of duplication typically rely on the reduction in staff numbers once the initiatives are implemented. These cost savings, while appearing reasonable in their quantum, will only be firmed up once discussions have been completed with Utility and City staff, and the required human resources protocol has been established as part of the implementation process. In the analysis below, we have excluded cost savings related to plant automation as this is presently being pursued by the City.

Based on a review of the items above, water and wastewater billing and collection could be realised through a contracting arrangement with the City and Utility, and is therefore not dependent upon integration.

6.2.4. Other Initiatives

The other initiative identified is an improvement in working capital, if monthly billing is adopted for water and wastewater, as opposed to semi-annual billing.

Currently, the City bills approximately $24 million annually for water and wastewater services. Approximately 75% of this total bill is for customers who are billed in arrears every six months (i.e. $18 million). The remaining bills for customers are already billed by the City on a monthly basis. Of the City's water and wastewater customers, GSU provides monthly billing for hydro services to approximately 60% (i.e. 27,000 out of a total of 44,000 customers). Thus, there are annual water and waste water bills

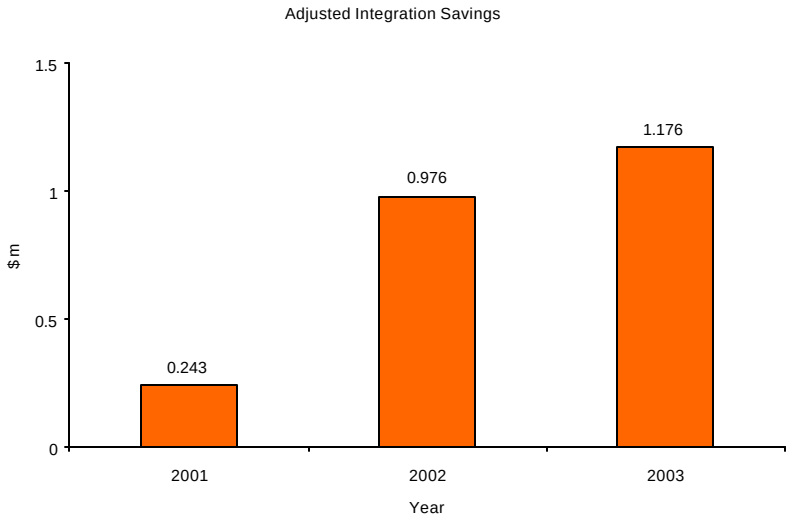
totalling $10.8 million annually (i.e. $18 million x 60%, or $900,000 monthly) which the City bills on a six monthly in arrears basis, which the integrated Utility could bill on a monthly basis at no extra cost.

Based on these figures, if the integrated Utility were to start billing on a monthly basis immediately, in the first month of billing one month in arrears, it would receive a one-off additional $2.25 million in cash. If the integrated Utility need only hold a similar level of cash as it had before, then this additional cash could be returned to the shareholder as a one-off payment. Alternatively, assuming a cost of capital of 6%, on an annual basis this would equate to an annual reduction in holding costs of approximately $130,000 or an annual additional return on capital of $130,000.

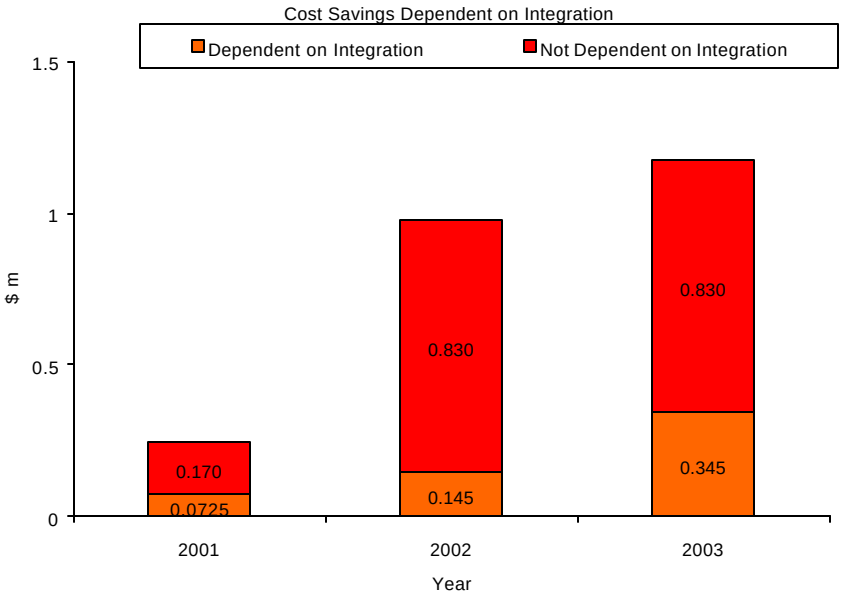
Assessment:
This initiative could be implemented irrespective of integration, provided there is cooperation with GSU in the provision of monthly billing.

6.2.5. Overall Assessment of Integration Savings

Adjusting the projections to remove the plant automation savings, the following savings are projected from integration.



Macquarie has been asked to comment on the ability to realise cost savings if the integrated model was not implemented. In this regard, we are in agreement with Navigant's assessment which stated the City would only achieve approximately two-thirds of the identified savings if water and electricity remained separate, but it could realise all of the savings if the operations were integrated. This is illustrated by the bar chart below which allocates the bar chart above between whether the annual savings are dependent upon integration or not according to the assessments made for each category.


Cost Savings Dependent on Integration
Dependent on Integration
Not Dependent on Integration
1.5
1
0.5
0
$ m
0.170
0.0725
0.830
0.145
0.830
0.345
2001
2002
2003
Year

7. Financial Implications for City

7.1. Introduction

This section discusses the expected distribution to the City from GSU.

7.2. Background

The capital structure of GSU implemented at its incorporation includes both equity and shareholder debt in the form of a promissory note. As a consequence, the City as shareholder is entitled to receive interest on the promissory note and dividends on the equity. The amount of dividends will depend on the policy established by the shareholder and Board of Directors, while the interest payments will depend on the principal amount and rate of interest set out in the promissory note.

The City in its 10 year capital plan is anticipating receiving $2.4 million (net) in interest payments from the promissory notes with GSU in 2001. This payment was projected at the time of GSU's incorporation based on:

- Electricity distribution rates not being increased;
- Historic operating performance of the Utility; and
- GSU being able to reduce operating costs by $1.5 million.

The figure of $2.4 million reflects the expectation that approximately $2.8 million would be available to be paid to the City but $400,000 needs to be retained to finance growth of the telecommunication business.

7.3. Ability to Pay Distribution to City

Based on information supplied by the Utility, it has met and exceeded its expectations for utility savings. One time transition costs, however are higher than anticipated at approximately $1.5 million. GSU has advised that the transition costs have been paid out of working capital.

With respect to the payment of the $2.4 million of interest to the City, the Utility has provided projections which indicate that after summer (when it receives a higher margin on energy sales) it will have sufficient working capital to make the interest payment to the City for 2001. The City and Utility still need to finalise the terms of the promissory note to establish the appropriate timing of payments to the City for this current year and for future years.

8. Implementation Plan and Timetable

8.1. Introduction

This section sets out the proposed approach and timetable that would apply to implement the model. An implementation plan and timetable will need to be continually revised and updated throughout the implementation process.

8.2. Implementation Tasks

A key principle for effective implementation of the model is the formation of a committed project team to be accountable for the implementation process. This project team would consist of senior representatives from the Utility and the City. The project team would be responsible for appointing any required consulting support.

Based on discussions with GSU staff, the implementation process is expected to include the following major tasks:

TASK	DESCRIPTION
1. Create the PUC	Establishment of Greater Sudbury PUC pursuant to a by-law which entrusts the water and wastewater infrastructure to the Commission
2. Develop Human Resources Protocol	Development of a human resources protocol to manage the transfer of City employees to Servicesco
3. Establish Corporate Governance	Establishment of an organisational and corporate governance model for the PUC including appointment of commissioners and reporting guidelines
4. Agree Rate Setting Framework	Establishment of a water and wastewater rate setting framework for the PUC to be approved by the City
5. Develop Services Agreements	Development of Services Agreements for the PUC with the City and Servicesco
6. Implement Operations Planning	Implementation of operations planning including: • Review of regulatory compliance issues • Establishment of benchmarking and performance measures • Meter shop amalgamation • Development of capital and operating budgets • Financial planning • Conversion of the billing system • Development of financial reporting systems

8.3. Timetable

Once an in-principle decision to adopt the integrated model is adopted by City Council, it is expected that these implementation tasks could be completed over a five month time period. Based on discussions with GSU staff, the broad timing for each task is set out in the timetable below.

	Month 1				Month 2				Month 3				Month 4				Month 5			
Week	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
Tasks																				
Create the PUC																				
Develop Human Resource Protocol																				
Establish Corporate Governance																				
Agree Rate Harmonisation and Setting Framework																				
Develop Service Agreements																				
Implement Operational Planning																				

This timetable appears reasonable if taken in isolation as it ensures adequate planning and preparation is directed to ensure that key issues are resolved and services levels are not jeopardised for customers during the transition. A comment was made by City staff that this timetable may be optimistic and a longer timetable maybe necessary as both the Utility and City are still working through the restructurings of last year. The competing demands of those processes could result in time delays.

8.4. Implementation Risks

There are a number of risks, examples of which are set out below, which need to be carefully managed to ensure that the integration benefits are realised.

- Loss of key staff during the restructuring;
- Excessive negative publicity;
- Industrial relations disputes;
- Failure to appoint competent change leaders for the transition;
- Failure to establish a comprehensive integration program;
- Failure to establish line management commitment to the integration program;
- Reduction in operational performance during the restructuring;
- Reduction in employee morale and support for the changes;
- Failure to realise integration benefits; and
- Poor management and coordination of the integration program.

A key risk, identified above, is a failure to realise the integration benefits. In order to manage this risk, the City and GSU need to actively monitor the integration performance and the ability to realise cost savings. It is suggested that the City and GSU should, if the model is approved by Council, jointly develop explicit criteria to ensure that the proposed objectives (including the projected cost savings) of the integrated model are achieved.

Appendix A - Sources of Information

Introduction

In preparing this Report, Macquarie:

- Reviewed documents produced by the Task Forces, Steering Committees, Working Groups, and Consultants, associated with the proposal to integrate electricity operations with water and wastewater services; and

- Interviewed with representatives from both the City and GSU.

A full list of documents reviewed and parties interviewed is set out below.

Documents

A list of documents reviewed include:

Task Force Reports

- Stage IV Report – Sudbury Hydro, Telecommunications Services (October 5, 2000)
- Utility Services Steering Committee Task Force – Stage 4, Engineering (Joint) Task Force, Geographical Information Systems (GIS) Services (May 11, 2000)
- Engineering Services GIS Services, Final Report, Stage 4 Completion of Business plans (11 May 2000)
- Operations Task Force, Draft Report Discussing the Amalgamations of the Three Municipally Owned Distribution Systems within the City of Greater Sudbury (May 1, 2000)
- Roads and Sidewalk maintenance Task Force Report (April 27, 2000)
- Addendum to Roads and Sidewalk Maintenance Task Force Report dated April 27, 2000 (Human Resource Impacts, Manpower Requirements, Organization Charts)
- Engineering Task Force Report (April 27, 2000)
- Addendum to Engineering Task Force (Human Resources Impacts) (April 27, 2000)
- Fleet Task Force Report (April 27,2000)
- Addendum to Fleet Task Force Report (Human Resources Requirements) (April 27, 2000)
- Stage IV - Completion of Business Plan, Greater Sudbury - Corporate Administrative Services (April 26, 2000)
- Customer Service Business Plan (May 11, 2000)

Navigant Reports and Presentations

- Assessment of Strategic Alternatives for City of Greater Sudbury Electric Utilities, by Navigant Consulting and Miller Thomson (June 16, 2000)
- Strategic Alternatives for City of Greater Sudbury Electric Utilities, by Navigant Consulting and Miller Thomson (Slide show dated June 19, 2000)
- Competitive Opportunities for City of Greater Sudbury Electric Utilities, By Navigant Consulting and Miller Thompson (June 16, 2000) (Compendium)

Other

- Greater Sudbury Utilities Inc., Summary
- Greater Sudbury Utilities, Presentation by Gary Polano (October 10, 2000)
- Shareholder Declaration for Greater Sudbury Utilities Inc.
- By-Law TB-33
- Promissory Notes (November 2000)
- 10 Year Capital Plan for City of Greater Sudbury

Interviews

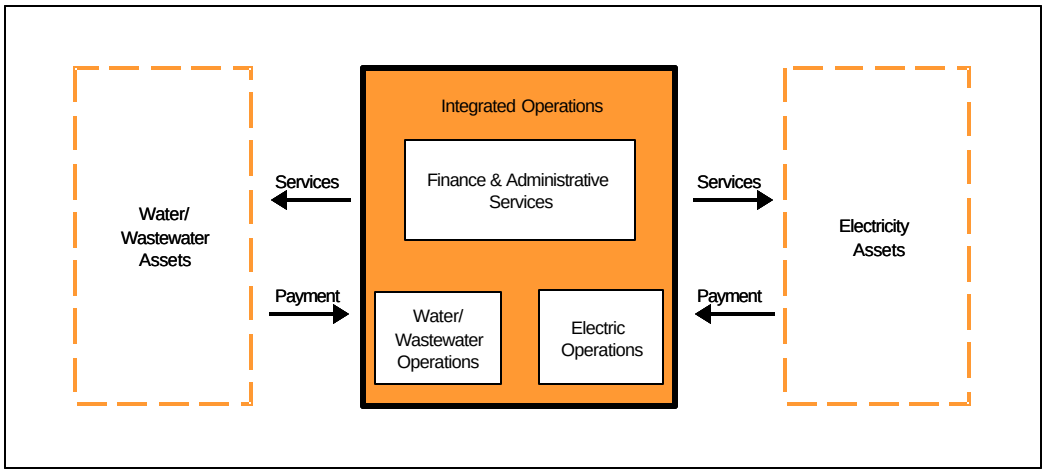
The parties interviewed by Macquarie include:

- Jim Rule, CAO, City of Greater Sudbury
- Don Belisle, General Manager, Public Works, City of Greater Sudbury
- Sandra Jonasson, Director of Finance, City of Greater Sudbury
- Kevin Shaw, Co-coordinator of Construction Services, City of Greater Sudbury
- Bob Falcioni, Operations, City of Greater Sudbury
- Ray Martin, Manager of Fleet, City of Greater Sudbury
- Kate Fyfe, Office Manager of Ontario Works, Greater Sudbury Utilities
- Stan Pawlowicz, CFO – Corporate Development & Resourcing, Greater Sudbury Utilities
- Daria Babaie, President & CEO, Greater Sudbury Utilities
- Doug Reeves, VP – Distributing Systems Services, Greater Sudbury Utilities
- Tom Trainor, Field Services Representative – Billing, Greater Sudbury Utilities
- Brain Cottam, Consultant

Appendix B – Navigant Conclusions on Integration Model

The following text is an extract from the executive summary of Navigant's report to the Transition Board – *"Assessment of Strategic Alternatives for City of Greater Sudbury Electric Utilities"*, June 16, 2000. (Please note that NCI/MT refers to Navigant).

> *NCI/MT were asked to comment on the potential advantages and disadvantages of integrating the City's water/wastewater and electric utility operations. Structurally, the integrated operations could comprise the staff and equipment from the respective organizations, with the water distribution and wastewater collection infrastructure being retained within the municipality and the electric distribution infrastructure being retained within the local distribution company. One possible structure for this integrated operation is shown in Figure 2.*



Integration of water/wastewater and electric utility operation into a single organization would;

- *Limit the municipality's liability and allow for separate insurance coverage.*
- *Provide the opportunity to take advantage of the business acumen and commercial orientation of the electric utility's Board of Directors.*
- *Change the water/wastewater budgeting process from a political decision to a business decision.*
- *Generate greater synergies than if the two organizations remained separate.*
- *Allow water/wastewater operations staff to support electric staff in an emergency and vice-versa.*
- *Provide an ideal platform to operate the gas distribution system if the City is successful in acquiring the gas franchise within the municipality.*

Water/wastewater staff suggest that a loss in synergies with the municipal roads group would be a disadvantage of the integration, but NCI/MT believe that most of these synergies can be retained through careful structuring of the relationship between the respective organizations and maintaining strong and effective working relationships. Another possible disadvantage would be harmonization of wage levels between municipal staff and CGS Hydro staff who are transferred in the integrated operations.

Based on NCI/MT's preliminary analysis, integration warrants further investigation.

Appendix C - Review of Utility Savings

Overview

Since its incorporation in November 2000, GSU has been actively pursuing internal restructuring initiatives centred around a voluntary exit program ("VEP"), and investigating opportunities for synergies between the City's operations and its own.

A recent review of these savings has resulted in adjustments to the amounts projected and new initiatives have been identified by the Utility. Overall this review indicates that the Utility is well on track in meeting and exceeding the Transition Board's cost savings projection. Based on the GSU's present projections, it is expecting to obtain cost savings of $1.78 million in 2001 increasing to $2.28 million by 2003 (as set out in the table below).

$000	2001	2002	2003
Initiatives Implemented or Underway			
• Initiatives Implemented	1,171	-	-
• Initiatives Ready for Implementation	321	-	-
Elimination of Outsourcing			
• Elimination of Outsourcing Arrangements	156	20	20
Shared Services with the City			
• Opportunities for Shared Services	-	259	-
Other Initiatives			
• Other initiatives	133	200	-
Total Savings	**1,781**	**479**	**20**
Cumulative Savings	**1,781**	**2,260**	**2,280**

Source: Greater Sudbury Utilities Inc.

A review of these revised projection is set out below for each category in the table above.

Initiatives Implemented or Underway

The costs savings from initiatives implemented primarily relate to seventeen staff members either accepting the VEP or retiring. A small portion of the savings relate to operating efficiencies related to the consolidation of the facilities of the three predecessor utilities.

In addition to the seventeen removed positions, a further six positions are currently in the process of being reduced – four through the VEP ($180,000 annual savings), one retirement of the locator and one associated operations position ($141,000 annual savings). The last two retirements will allow the Utility to contract for locates services at a much cheaper rate than it could provide the services internally.

In implementing these initiatives, one-off transition costs totalling $1.557 million have been or will be incurred by the Utility relating to termination benefits (i.e., accrued long service leave, holiday pay and redundancy payments). These transition costs have been funded out of GSU's working capital.

Assessment:
Given that these cost savings have been implemented or are close to being implemented, there is a high degree of confidence that these savings will be achieved in 2001.

Elimination of Outsourcing

In investigating opportunities for cost savings between the City and Utility's operations, there are a number of services currently outsourced to external parties by either the City or the Utility which could be performed by the Utility or the City within their existing resources. This would result in cash flow, previously paid to the external parties, being paid to the Utility or the City. This would result in cash flow being retained within the community rather than being paid to external parties where there is no opportunity to retain any proportion of the cash flow within the City or Utility.

The identified opportunities for elimination of outsourcing arrangements relate to:

- ***Street lighting services*** – the Utility is investigating providing street lighting maintenance services to areas where an external contractor provides these services for the City ($56,000 annual savings).

- ***Garaging*** – the Utility is investigating providing garaging and maintenance services to the fire service vehicles (annual savings of $60,000 in 2001, with an additional $20,000 in each of 2002 and 2003).

- ***Body Work*** – the Utility is investigating arranging for the City to do body work on GSU vehicles. This work is currently being outsourced to external parties ($15,000 annual savings). This may be contingent upon the present restructuring of fleet services for the municipality.

- ***Legal*** – the Utility is proposing using certain municipal legal services rather than outsourcing to external providers ($25,000 annual savings). We have been advised that the City could not perform these services without incurring extra costs.

The City has indicated that it is willing to consider contracting services to the Utility or providing services to the Utility on condition that:

- any contracts do not result in an increase in costs for the City (i.e., the Utility has excess capacity in its existing operations);

- any contracts include flexibility and performance measures such that the City is not locked into any rigid arrangements; and

- any contracts are tested against the market to ensure that the City is receiving best value.

Assessment:
These initiatives apart from legal appear relatively straightforward and should be progressed, where practical, by the City and Utility. There is nothing to suggest that these cost savings could not be achieved timeframes anticipated by GSU nor would they result in any increased costs to the City.

Shared Services with the City

Another category of cost saving is the potential for the City to perform certain administrative services for the Utility which it presently performs for its own operations. If the City is willing to perform these services, the Utility is able to downsize its administration department and revenue would be provided to the City for providing the services. That is, in some circumstances the Utility would realise cost savings for no longer having to provide a service and the City would receive a revenue for providing the service. In the numbers below, the increase in revenue for the City has been added to the savings for the Utility. By way of example,

the Utility intends to outsource its company secretarial work to the City. This is anticipated to save the Utility $60,000 per annum (net of new outsourcing costs) and result in a payment to the City of $20,000 per annum. The Utility records the total cost savings as the net benefit of the two items (i.e., $80,000).

The identified administration functions relate to:

- Purchasing Services ($57,000 = $34,000 savings to Utility and $23,000 revenue to City);
- Payroll ($40,000 = $20,000 savings to Utility and $20,000 revenue to City);
- Human Resources ($60,000);
- Corporate Secretary Services ($80,000 = $60,000 savings to Utility and $20,000 revenue to City); and
- Facilities Management ($22,000).

The ability to implement these initiatives requires further investigation by the Utility and City. This is because collective agreements for existing Utility staff appear to have restrictions upon the contracting out of utility services to third parties. In addition, the City and Utility do not appear to have had substantive discussions about the City's willingness to provide these services on the terms (including price) proposed by GSU.

Assessment:
These initiatives require further investigation to resolve the collective agreement restrictions before it can be determined with confidence that these cost savings are achievable. As a consequence, we have removed the estimates for shared service savings from the projections for prudence. If these savings can be realised, it will represent upside for the Utility and City.

Other Initiatives
In addition to the categories above, there are a number of other initiatives which have been identified which are broadly categorised as "other". These initiatives include:

- ***Meter readings*** – shifting meter readings to quarterly time period from monthly (which is in line with industry standards). This would result in savings of $100,000 per annum which can be implemented in 2002 once the existing meter reading contract expires. This proposal appears straightforward provided it can be achieved without any disruption to customers though the estimations process between readings.
- ***Consolidate call centre service for City and Utility*** - GSU has a similar call centre while the municipality is currently in the process of opening a call centre. Savings of $100,000 from 2002 could be achieved if there was an ability to reduce staffing levels through a combined call centre. This option requires further investigation at both the Utility and municipal level to see whether consolidation of call centre services is feasible.
- ***Reduced cost for maintenance construction*** – this proposal has an estimated savings of $53,000 per annum.
- ***New revenue opportunities*** – the Utility has identified new revenue opportunities out of the distribution system code. These opportunities, once approved by the Ontario Energy Board, are estimated to result in additional revenue of $80,000 per annum to GSU. This is not a cost saving but rather a increase revenue to the Utility in the ordinary course of business, rather than as a result of restructuring initiatives.

There are also a number of preliminary initiatives being pursued by the Utility which have not yet resulted in identified costs savings. These initiatives, which could result in future savings, relate to:

- A Utility review of existing operations to identify business process improvements; and
- Opportunities for the Utility to provide energy management services to the City's facilities.

Assessment:
Overall, there are opportunities for cost savings from this "other" category especially from changing the frequency of meter readings and the reduction of a maintenance construction worker. Other cost savings related to consolidating the call centres, require further investigation before they can be included with confidence in the projections. As a consequence, we have removed estimates for consolidating the call centres and the estimates for new revenue as it is not directly related to the restructuring initiative.

Overall Assessment

Based on the assessments made above, certain cost savings have been excluded from the revised projections provided by the Utility. Notwithstanding these exclusions, GSU has been successful in implementing cost savings initiatives primarily from the reduction of staff positions. Based on the adjusted revised projections, GSU is on track to meet the expectations for costs savings from the restructuring of GSU. In addition, there is the ability to exceed these savings levels, if other savings initiatives and shared service initiatives (which require further investigation) can be implemented.