Electric Franchise Fee Discussion Paper

Purpose

The purpose of this paper is to introduce/re-introduce committee members to the City of St. Albert's Electrical Franchise agreement with FortisAlberta for Council to explore potential implementation of a franchise fee after considering the benefits, drawbacks and options.

Franchise Agreement

A "franchise agreement" is a common tool used by municipalities across the province. While some municipalities own and regulate their utility distribution systems, most municipalities enter into a franchise agreement with a utility distribution or transmission company to build, own, operate and maintain the distribution system that services their community.

These agreements:

- Grant a utility distribution or transmission company the use of municipal rights-of-way;
- Allow a utility distribution or transmission company the right to construct, operate and maintain the utility distribution system within the municipality;
- Identify core services to be provided;
- Outline standards of maintenance and performance measurement;
- Specify franchise fee calculations, to be charged by the municipality to the company for the right to use municipal rights-of-way and as compensation for the loss of taxable property due to utility corridors; and
- Provide for dispute resolution mechanisms and other terms of agreement.

PREVIOUSLY DISTRIBUTED

The legal authority for franchise agreements and fees within the Municipal Government Act (MGA) resides in:

- Section 45(2) noting that a council "may grant a right, exclusive or otherwise, to use the municipality's property, including property under the direction, control and management of the municipality, for the construction, operation and extension of a public utility in the municipality for not more than 20 years";
- Section 61(2) states that "a municipality may charge fees, tolls and charges for the use of its property";
- Section 360(1) details the legal authority where "a council may make a tax agreement with an operator of a public utility" and;
- Section 360(2) indicates that "Instead of paying the tax imposed under the Division and any other fees or charges payable to the municipality, the tax agreement may

provide for an annual payment to the municipality by the operator calculated as provided in the agreement".

Franchise Fee/ Local Access Fee

A franchise fee is an amount paid to the municipality to use their infrastructure. It is basically a payment, partially in lieu of forgone taxes on property due to the use of utility corridors. The electrical distribution company bills and collects the franchise fee from customers and they would in turn send payments to the municipality. The amounts billed to customers are based on the agreed fee calculation within the franchise agreement and bylaw.

Municipal Franchise Fees or Local Access Fees (LAF) are also known as Municipal Consent and Access Fee (MCAF). As the fees vary across the province, the local access fees tend to be a mechanism for municipalities that own and regulate their electric distribution system. While various terms are used across the province, they are essentially referring to a similar fee.

Electric franchise fee calculation

A franchise fee can be calculated as a percentage of the cost of the commodity plus a company's delivery revenue, or based only on delivery revenue. St. Albert's electric franchise agreement provides that the fees be based solely on actual delivery revenue. This ensures that the fee amount does not rise or fall with the cost of the electricity commodity and therefore rate stability is maintained.

PREVIOUSLY DISTRIBUTED

Alberta Utilities Commission (AUC) Fee Ceiling

The Alberta Utilities Commission Act sets a fee ceiling of 20%**.** Municipalities may select a franchise fee within their franchise agreement anywhere between 0% and 20%. Through designated processes, Council may seek to adjust the franchise fee on an annual basis, below the ceiling, periodically during the agreement without seeking the approval of the AUC. The 20% fee ceiling cannot be exceeded without prior approval from the AUC Board.

The City has the option to adjust its franchise fee rate in the electric franchise agreement by providing written notice to FortisAlberta no later than November 1st of each year preceding the planned change. The City is also required to provide local notice of its intent to change the level of the franchise fee, at least 45 days prior to the implementation of the revised rate; for example a process to amend the 2019 franchise fee would need to commence prior to October 2018, if such a fee was being contemplated by Council.

Benefits of Franchise Fees

The application of franchise fees has a number of important benefits for Canadian municipalities. Some of these benefits include:

1. Provincial and regional consistency and comparability would be enhanced. Many municipalities in Alberta and in the Edmonton Metropolitan Region specifically have elected to charge franchise fees. These municipalities utilize the fee revenue as a means of funding various programs and services and/or to keep their property taxation rates competitive. To truly compare the cost of living/doing business in a municipality, one must consider the sum of all revenue streams and costs including taxation, user fees (ie. Franchise fees), utility rates, land costs, servicing costs etc.

2. A reliable and growing revenue stream would allow the City to :

    - Re-position the City's revenue structure allowing for future property tax increases to be minimized.

    - In 2016, property taxation accounted for approximately 54% of St. Albert's total revenue (excluding government transfers) as shown in Appendix A. One way to reduce this reliance is to pursue diversification, such as an increased focus on non-tax sources like user fees, franchise fees, etc.

3. A "user pay" system has a number of economic benefits compared to traditional property taxation.

    - User fees are considered a more flexible alternative for ratepayers compared to property taxes because consumers would have some control over the incidence of a franchise fee through their ability to manage electricity consumption. Property taxes offer no such flexibility and are generally considered regressive in nature.

4. Franchise fees allow the City to receive compensation for loss of taxable property and granting exclusive right of way access.

    - A franchise agreement provides a company with use of municipal rights of way within the service area and the exclusive right to deliver the service to the community. Compensation relative to this access and for the loss of taxable property due to utility corridors is considered prudent, as these costs should not be accommodated by property taxes.

PREVIOUSLY DISTRIBUTED

- Essentially, when a utility company uses private land, it pays rent to the landowner (municipality) and passes along this "cost of doing business" to the end consumer

5. A "user pay" system also has non-economic benefits such as the encouragement of conservation.

   - Economic principles suggest that an increase in the price of a product or service will drive the quantity demanded down – more simply, user fees serve to discourage inappropriate consumption or waste.

6. Franchise Fees are supported by the City's provincial association, and are not considered a "tax".

   - The *Alberta Urban Municipalities Association* (AUMA) supports the right of municipalities to charge franchise fees and supports the principle that franchise fees are not taxes. The City currently uses the AUMA's standard franchise agreements.
   - The *Alberta Utilities Commission* also takes the position that franchise fees are not taxes. In various judgments, including the Town of Bow Island's 2008 rate decision, the Board repeated that it "considers that a franchise fee is a user fee." Franchise fees are considered, essentially, a cost of doing business.
   - Transparency also exists, as all municipal budgets are approved in public and include the amount raised through franchise fees and property taxes. Fees are also clearly indicated on utility bills.

PREVIOUSLY DISTRIBUTED

Drawbacks of Franchise Fees

In addition to the benefits, franchise fees have a number of characteristics that a Council should consider prior to considering implementation. These include:

1. Consumer utility bills would be affected.

   Utility companies apply the cost of municipal franchise fees to consumer utility bills. This would result in a marginal increase to electrical bills in the community. For a household with average monthly power consumption of (600 kWh), at a rate of 10%, the increase in the electricity bill would be approximately $6 per month or $73 per year based on estimated 2018 rates. Details of the impact on utility rates for residential and non-residential consumers are illustrated in the “Impact on Electrical Rates” section located on page 8.

2. Institutional and not-for-profit facilities would not realize the benefit of minimized tax increases.

   Facilities such as churches, schools, and other not-for-profit facilities would bear an increased utility bill burden from a franchise fee. These facilities would not benefit from minimized property taxation, as they are exempt from property taxation pursuant to provincial legislation.

PREVIOUSLY DISTRIBUTED

Electrical Franchise Fees in Alberta

Of about 300 communities in Alberta that are serviced by electricity distributors, primarily ATCO Electric and FortisAlberta, 69% of communities have a franchise fee rate from 0.50% to 20%. These Rates and Tariffs schedules that denote the fees that different municipalities use are posted on the electricity distributors’ website and a summary of rates for small to mid-size municipalities are outlined in Appendix B & C. The remaining 31% of municipalities have a franchise fee at 0%. For the smaller size municipalities, with a population range from 10,000 to 60,000, 90% of the municipalities have a franchise fee, with the exception of Fort Saskatchewan and Mackenzie.

Among the six midsize municipalities, three municipalities (Red Deer, Lethbridge and Medicine Hat) own and operate their own electricity distribution system. It is difficult to compare these municipalities against St. Albert given that the electricity components of their business invariably generate levels of profit over and above whatever franchise fee they may or may not charge, which ultimately impacts the comparability of property tax rates.

The remaining three midsize municipalities (including St. Albert) manage their electricity distribution through a franchise agreement and franchise fees range from 0% to 13%

Electrical Franchise Fee Rates for Midsize Municipalities
(By population - Highest to lowest)

Municipality	Franchise Fee/ Local Access Fee	Effective Date of Rate	2016 Population
City of Red Deer	12.93%	3/1/2017	99,832
City of Lethbridge	16.50%	1/1/2018	96,828
City of Grande Prairie	7.75%	3/1/2011	68,556
City of St. Albert	0.00%	1/1/2016	64,645
City of Medicine Hat	0.00%	1/1/2016	63,018
City of Airdrie	13.00%	1/1/2016	61,842

Sources of Data:
Population data from 2016 Municipal Affairs Population List
Franchise fee and Local Access Fee data provided by FortisAlberta, ATCO Electric, municipalities, and the Utilities Consumer Advocate

PREVIOUSLY DISTRIBUTED

Red Deer and Lethbridge own and operate their own electricity distribution company, but have elected to also levy a local access fee, whereas Medicine Hat does not have a fee, despite having control and ownership of their electricity distribution company. Overall dividends/profits from these system are not easily ascertainable.

At the current franchise rate of 0%, St. Albert's electric franchise fee is not in-line with other similar size communities.

Electrical Franchise Fees in St. Albert

History

Many municipalities in Alberta have municipal electrical franchise agreements in place, including the City of St. Albert. On November 15, 1928 Council entered into a franchise agreement with Calgary Power Ltd. to grant the company a special franchise to supply electricity to what was then the Town of St. Albert and its residents. The agreement did not incorporate a franchise fee.

In 2001, Council resolved to require an 8% franchise fee within its electric franchise agreement, accompanied by a corresponding reduction in municipal property taxes. The effective date of the franchise fee was September 1, 2001. Subsequently, a change in Council resulted in a decision reversal.

In 2002, the City signed a franchise agreement with "Utilicorp Networks Canada (Alberta) Ltd." (now "FortisAlberta") and approved by bylaw. The bylaw/agreement was in a form prepared by the Alberta Urban Municipalities Association (AUMA) and used by numerous municipalities across the province.

In 2015, due to a change in the agreement template by AUMA, which was revised after consultation with various local authorities and utility companies, including FortisAlberta and ATCO Electric, St. Albert adopted the new template and the electrical franchise agreement with FortisAlberta was executed in 2015 that repealed bylaw 31/2001, following approval of the bylaw 17/2015.

The following table illustrates the estimated revenue potential for the City of St. Albert should an electrical franchise fee be implement at varying levels:

Electrical Franchise Fee %	Franchise Fee Amount
3.0%	940,061
5.0%	1,566,768
8.0%	2,506,829
10.0%	3,133,536
15.0%	4,700,304
20.0%	6,267,072

PREVIOUSLY DISTRIBUTED

Effect to Residents and Businesses:

In the event that Council does proceed to implement a franchise fee, residential consumers would see a slight increase and the resulting impact on their utility bills. To the extent that consumers can curb electricity usage, the increase of utility costs may be minimized. A franchise fee of 10% and average monthly residential consumption of 600 kWh will result in an annual fee of $73.

Franchise fees are designed to generate income from a different customer base and are an additional/alternate revenue source for the municipality. Institutional and not-for-profit facilities such as churches, schools and other not-for-profit facilities, including federal and provincial government, would bear an increased utility bill burden from a franchise fee, as they are exempt from property taxation by provincial legislation. The use of franchise fees to increase revenue from tax exempt groups ensures that the burden of paying for City services is more equitable.

A Carbon Tax Levy was introduced by the province in 2017 on gas, diesel and propane. While the actual carbon tax is not charged on electricity per se, electricity producers are subject to the Specified Gas Emitters Regulation (SGER). This regulation ultimately represents an increase on overall electrical bills to customers. While there is no further increases being communicated by the province at this time, there is always potential for this to change in the future. These components, while outside of the City's control, may pose sensitivity to any utility increase to end users.

Impact on Electrical Rates

The following charts are presented for illustrative purposes to demonstrate the potential impact on both residential and non-residential users and are calculated based on an estimating tool provided by Fortis Alberta. Actual charges for any individual customer are calculated based on actual delivery costs on that specific account as well as the specific rate category that the customer belongs to.

PREVIOUSLY DISTRIBUTED

Impact on Utility Rates - Residential

Residential		Selected Franchise Fee Amounts					
Usage Estimate		**3% Monthly**	**5% Monthly**	**8% Monthly**	**10% Monthly**	**15% Monthly**	**20% Monthly**
Low use	400 kWh	$1.45	$2.42	$3.87	$4.84	$7.26	$9.67
Mid use	600 kWh	$1.82	$3.03	$4.85	$6.06	$9.09	$12.13
High use	800 kWh	$2.19	$3.64	$5.83	$7.29	$10.93	$14.58

Impact on Utility Rates - Non-Residential

Non-Residential - Small Commercial		Selected Franchise Fee Amounts					
Usage Estimate		**3% Monthly**	**5% Monthly**	**8% Monthly**	**10% Monthly**	**15% Monthly**	**20% Monthly**
Low use	1,000 kWh	$32.07	$53.46	$85.53	$106.91	$160.37	$213.83
Mid use	2,500 kWh	$79.32	$132.21	$211.53	$264.41	$396.62	$528.83
High use	5,000 kWh	$158.07	$263.46	$421.53	$526.91	$790.37	$1,053.83

*the categories selected above are based on actual average usage for St. Albert customers

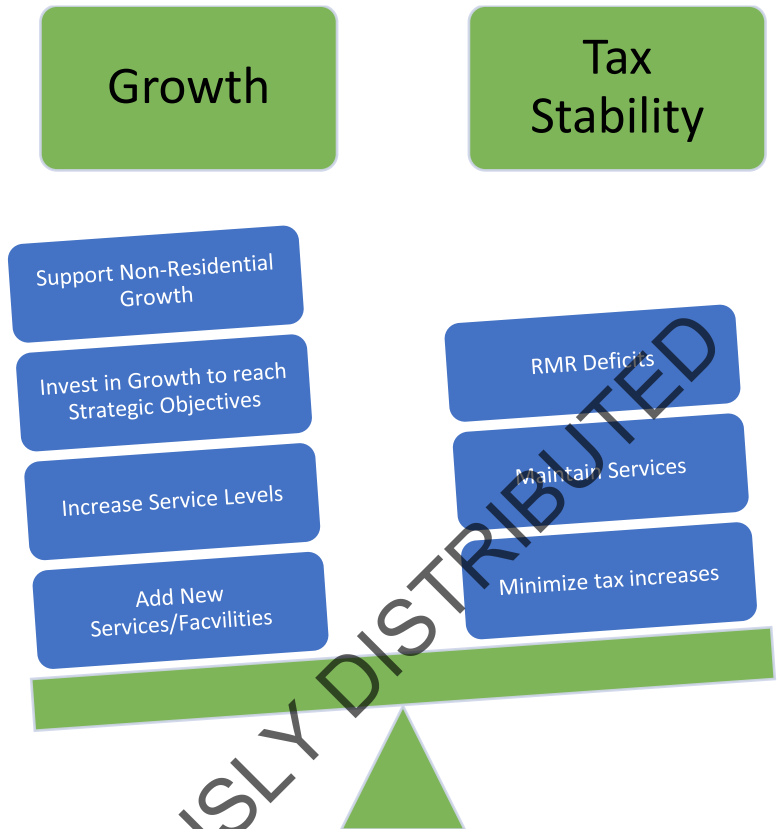
Options For Use of Franchise Fee Revenue

Should the City of St. Albert choose to implement an electrical franchise fee at Council's prerogative, there are a multitude of uses and applications for the additional revenue. The options span an entire spectrum and consideration should be given to the long term needs of the community and Council's Strategic Plan.

There will always be competing priorities for the municipality some of which include:

- minimizing tax increases
- addition of new services
- increases to service levels

- supporting non-residential economic development
- investing in needed capital growth projects



PREVIOUSLY DISTRIBUTED

Process for implementation of a franchise fee

Should Council wish to implement a franchise fee, there are a number of steps in the process. Each year Council has the opportunity to amend the franchise fee through a bylaw update when all the criteria below have been met.

1. Council passes a motion to approve the increase in rate;
2. Submit written notice to FortisAlberta no later than November 1st of the year preceding the planned change;
3. Place an advertisement in the St. Albert Gazette to solicit resident response, at least 45 days prior to the implementation of the revised rate. Responses are collected for 14 days;
4. Once the advertising is done, there is a 45 day waiting period for objections. If there are no objections, Fortis Alberta will then file the application with the Alberta Utilities Commission (AUC) for approval;

5. Passing of an amending bylaw to update the fee.

Conclusion

St. Albert currently does not impose an electrical franchise fee. As a large percentage of municipalities in Alberta take advantage of this revenue diversification strategy, it is misleading when comparing property tax levels between communities.

Should Council wish to pursue this strategy, Administration could provide further analysis and recommendations regarding choice of rates, phasing options and options for the application of revenue.

PREVIOUSLY DISTRIBUTED

Report Date: February 12, 2018
Author(s): Monica Chan, Senior Financial Analyst
Committee/Department: Financial Services

APPENDIX A

Property Taxes Revenue

($ Thousand)

		2012	2013	2014	2015	2016
	Total Revenue	168,588	193,202	181,612	204,641	200,750
Less:	Government Transfers	(27,533)	(37,365)	(24,401)	(21,684)	(27,140)
	Adjusted Revenue	141,055	155,837	157,211	182,957	173,610
	Property Taxes	77,533	81,648	85,161	90,691	93,123
	% of Adjusted Revenue	55%	52%	54%	50%	54%
	Average 5 Year Property Taxes					**53%**

Source: 2012 -2016 Annual Reports

PREVIOUSLY DISTRIBUTED

APPENDIX B

Electrical Franchise Fee Rates for Midsize Municipalities

(By population - Highest to lowest)

Municipality	Franchise Fee/ Local Access Fee	Effective Date of Rate	2016 Population
City of Red Deer	12.93%	3/1/2017	99,832
City of Lethbridge	16.50%	1/1/2018	96,828
City of Grande Prairie	7.75%	3/1/2011	68,556
City of St. Albert	0.00%	1/1/2016	64,645
City of Medicine Hat	0.00%	1/1/2016	63,018
City of Airdrie	13.00%	1/1/2016	61,842

Sources of Data:

Population data from 2016 Municipal Affairs Population List

Franchise fee and Local Access Fee data provided by FortisAlberta, ATCO Electric, municipalities, and the Utilities Consumer Advocate

Notes:

1. Franchise fee rates range from 0% to 16.5% for midsize communities.
2. Red Deer, and Lethbridge own their own electricity distribution company, but have elected to levy a Local Access Fee.
3. Red Deer's Local Access Fees are calculated on distribution and energy charges.
4. Lethbridge's Local Access Fees are calculated on distribution and transmission charges.
5. Medicine Hat own and operate their electric distribution system however do not charge a fee.

PREVIOUSLY DISTRIBUTED

APPENDIX C Municipal Franchise Fees for Smaller Municipalities

Region	Franchise Rate	Effective Date	2016 Population
Spruce Grove	20.00%	1/1/2016	33,640
Leduc	16.00%	1/1/2014	30,498
Okotoks	10.00%	1/1/2017	28,016
Cochrane	15.00%	1/1/2015	25,122
Fort Saskatchewan	0.00%	10/1/2013	24,569
Grande Prairie			20,347
Lloydminster	11.00%	1/1/2015	19,740
Chestermere	11.50%	1/1/2014	19,715
Camrose	10.00%	1/1/2016	18,044
Beaumont	5.00%	10/1/2013	17,720
Stony Plain	20.00%	1/1/2015	16,127
Cold Lake	4.25%	1/1/2003	15,736
Sylvan Lake	12.00%	1/1/2016	14,310
Brooks	12.63%	1/1/2015	14,185
Strathmore	13.50%	4/1/2017	13,327
Canmore	10.00%	1/1/2016	13,077
High River	20.00%	7/1/2015	12,920
Lacombe	6.20%	10/1/2013	12,728
Wetaskiwin	12.00%	1/1/2016	12,621
Mackenzie	0.00%		11,750
Whitecourt	2.55%	1/1/2018	10,574

PREVIOUSLY DISTRIBUTED