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M A N I T O B A) Order No. 76/07
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THE PUBLIC UTILITIES BOARD ACT) June 1, 2007

BEFORE: Graham Lane, C.A., Chairman
Susan Proven, P.H.Ec., Member
Monica Girouard, C.G.A., Member

THE TOWN OF SOURIS
REVISED WATER AND SEWER RATES
EFFECTIVE JULY 1, 2007

Executive Summary

By this Order, the Public Utilities Board (Board) varies an application of the Town of Souris (Town) for revised water and sewer rates. While the Board accepts the Town's three-year rate proposal, it establishes amended 2007 rates effective with an earlier than proposed implementation date, being July 1, 2007.

Minimum quarterly bills for residential customers will increase from \$40.45 to \$46.70 on July 1, 2007 (a 15.45% increase), then increase to \$54.10 on January 1, 2008 (a further increase of 15.84%), and to \$59.20 on January 1, 2009 (another increase of 9.43%). The overall increase over a thirty-month period is 46.35%. Bulk water rates will not change, having been substantially increased in 2003.

Although the rate increases are very large and represent rate shock (the dollar increase over current prices after the 2008 increase is implemented will be \$18.75 per quarter, or \$75.00 per year), they are necessary and represent the minimum required recognizing the significant upgrading required in upcoming years.

The Town's current Utility surplus and reserve balances are far too low to meet known and unexpected challenges to come, and combined with the fourteen year period since the last increase in 1993, provide the rationale for the large adjustments. Municipal utilities are expected to break even on operations and

if not, are expected to provide for recovery immediately.

While operating deficits were projected for 2007 and 2008, even after reflecting the proposed increases; the Board expects that by implementing the 2007 increases earlier than proposed, the deficits will be lower than projected.

Given the age and condition of the Town's utility infrastructure, and the upgrading that is required, and despite the increases now provided, the Board expects further significant rate increases will eventually be required. Accordingly, and to allow the Board to monitor developments, the Board requires the Town to file its utility financial statements for the years ending December 31, 2007, 2008 and 2009 with the Board, together with commentary on the upgrading program and rate adequacy.

Application

On March 8, 2007, the Town applied to the Board for revised water and sewer rates, as set out in Town By-law No. 1820. The Town proposed a three year phase-in of sharply increased rates, though with the first increase to take effect October 1, 2007 rather than the July 1, 2007 date now set by the Board. In summary, the Town's rate proposal recognized increased costs of utility operations and provided for the future upgrading of its ageing infrastructure.

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A public hearing was held at the Memorial Complex in the Town of Souris at 7:00 p.m. on May 10, 2007. Despite Notice of Hearing being provided to the public, only representatives of the Town and the Board were present.

Rates were last amended in 1993; existing and proposed rates were:

Step Rates (\$/100 cubic feet) ⁽¹⁾	<u>Existing</u>		<u>Proposed</u>					
			2007		2008		2009	
	Water	Sewer	Water	Sewer	Water	Sewer	Water	Sewer
1 st First 2500	\$3.50	\$2.02	\$4.20	\$2.42	\$5.04	\$2.91	\$5.59	\$3.23
2 nd Next 22,500	\$3.22	\$2.02	\$3.86	\$2.42	\$4.64	\$2.91	\$5.15	\$3.23
3 rd Next 75,000/over 25,000	\$2.97	\$2.02	\$3.56	\$2.42	\$4.28	\$2.91	\$4.75	\$3.23
4 th Over 100,000	\$1.10	\$2.02						

Note¹ The proposal is to eliminate the 4th step; the 3rd step would include all consumption over 25,000 cubic feet.

Residential Minimum Quarterly Bill (5/8" meter)	\$40.45	\$46.70	\$54.10	\$59.20
Service Charges	\$12.85	\$13.60	\$14.35	\$15.10
Bulk water (\$/1,000 gallons) ⁽²⁾	\$16.50 ⁽³⁾	\$16.50	\$16.50	\$16.50

Note⁽²⁾ The bulk water rate last approved by the Board was \$5.50 per 1,000 gallons. Without approval, the Town revised the rate to \$16.50 on November 1, 2003.

Note⁽³⁾ Equates to \$10.31/100 cubic feet

In its proposal, the Town proposed the deletion of the 4th rate step from its rate schedule. Since the closure of the cheese factory in 2003, no customer buys water at the former 4th rate step volume, making the step redundant. The Town also proposed to reduce the volume cap for the 3rd rate step from 75,000 cubic feet to 25,000 cubic feet. This would reduce the cost of water for higher volume users, and mitigate the effect of the overall rate increases for those customers.

By-law No. 1820 established other utility provisions, these related to hydrant rental charges, late payment charges, service beyond the Town's boundaries, sewer surcharges and others typical of those established for the utilities of other Manitoba municipalities, and acceptable to the Board.

In support of its application, the Town submitted a rate study prepared by Meyers Norris Penny, an accounting firm. The Town also responded to questions filed with the Town by the Board in advance of the hearing.

The Town's utility operating expenses projected for 2009 were reflected in the Town's rate proposal, as were the intended \$25,000 annual contribution to the utility reserve fund, and \$55,372 annual provision for contingencies (not all repairs or enhancements to be carried out through to 2009 can be known at this time). The proposal also reflected an expectation of normal general inflation through the 2007-2009 forecast period.

Administration	\$ 47,847
Water	\$282,995
Sewer	\$122,364
Reserves	\$ 25,000
Contingency Allowance	<u>\$ 55,372</u>
Total	<u>\$533,578</u>

Based on these projected expenditures and reserve contributions, the overall 46% increase in residential minimum quarterly bills by 2009 was indicated as being required.

Unaccounted for Water

Unaccounted for water, water produced and treated but not billed, was approximately 41% in 2006. Such water may have been lost through water main leaks, system flushing and hydrant use. The Town advised that the level of unaccounted for water in 2006 level was attributable to a water main break that went undetected for some time. The expectation for 2007 and future years was for much lower levels of unaccounted for water. While the Town has not experienced a shortage of water, the costs of producing and treating water that is lost is high and water loss is contrary to the goals of conservation.

Deficit Forecast

Under the Town's proposal, even with the proposed increases implemented, operating deficits may be expected in 2007 and 2008. The Town projected deficits of \$97,818 and \$37,631 for 2007 and 2008, with a small surplus of \$1,407 for 2009. Projections of deficit and surplus depend upon actual experience.

Utility Capital Expenditure Plans

The Town advised its wastewater treatment plant (WTP) required significant upgrades, with the 2004 total cost estimate of approximately \$2.9 Million; construction costs have experienced

considerable inflation since 2004. The Town plans to proceed with the upgrading in phases. Phase 1 was projected to cost \$500,000, to be funded by contributions from the Town (\$233,000) and the Federal and Provincial governments (\$133,000 each).

Beside the expected WTP upgrades, the following additional annual capital expenditures were forecast, and relate to replacement of mains and services:

2007	\$ 80,229
2008	\$201,920
2009	\$115,863
2010	\$ 72,545
2011	\$ 91,166

Further, an additional project for Glenwood Street North is expected to cost \$259,035.

Funding of Capital Projects

The cost of the original water and sewer system was funded in part through the issuance of Town debentures, with the annual servicing costs for the debenture met through levies on the Town's general tax base, and not through utility rates. As the Town has approached the limits of its municipal borrowing capacity, the ability to borrow to finance utility capital expenditures was reported to be limited.

While the Town plans to seek senior government and Manitoba Water Services Board (MWSB) grants to assist with funding the upcoming capital projects, the remainder may have to be raised

through rates.

Criticism of the Proposal

Ahead of the hearing, a ratepayer provided criticism of the Town's rate proposals, focused on the bulk water rate, the rate charged to system connected customers outside the Town limits, and the rates charged to low-pressure sewer customers.

The ratepayer was concerned with rate fairness, claiming that bulk water rates were not high enough and did not provide any contribution to the utility capital costs borne by Town residents through tax levies.

The Town responded that following the 2003 increase in bulk water rates from \$5.50 per thousand gallons to \$16.50 per thousand gallons, bulk water users were contributing to system capital costs. The Town further noted that as a result of the increase some bulk water customers have since chosen to purchase water from other suppliers. The Board understands that in 2006 only 1.4% of total sales were of bulk water.

With respect to the ratepayer's concern over connection charge fairness, the Town reported that all customers pay for connections, and that a local improvement levy of \$145.78 is collected from these customers towards the capital costs of the water treatment plant. The Town also advised that connected sewer customers will be assessed a portion of the capital costs

of the wastewater treatment plant upgrade, following the completion of the project.

With respect to ratepayers criticism of the approach taken to low-pressure sewer customers (low-pressure system customers are responsible for pump-out and sewage hauling costs), being billed the same rates as full sewer service customers despite a lower level of service, the Town defended its approach.

The Town advised that the low-pressure system service was put into service at a time when the Town had limited borrowing capacity and was unable to expend the funds necessary to provide full sewer service to, now, about 60 customers. The Board understands that the topography of the location of the low-pressure service was a factor in the development of the dual system, which has been in place for about thirty years.

The Town provided justification for the present approach, indicating that:

- a) sewage hauled to the wastewater facility from customers on the low-pressure system is non-aerobic or septic, requiring special treatment to provide for proper decomposition, incurring costs not present with the treatment of sewage from the other sewer customers (liquid and solid gravity-flow system);
- b) sewage from the low-pressure system contributes to more wear and tear on the wastewater facility;
- c) no charge is levied by the Town on low-pressure sewer

- customers hauling solid waste to the wastewater facility;
- d) the connection fee for low-pressure customers, \$63.00 per foot, is lower than the \$67.00 charge assessed gravity flow customers; and
 - e) the kind of sewer service provided is determined by the system in place, and customers of the low-pressure system are aware of and generally accepting of the current approach.

Concluding Comments

The Town advised the Board that while the application proposed an October 1, 2007 rate increase implementation, sooner approval would allow the utility to meet its objectives earlier.

The Town acknowledged that its past practice of infrequent rate reviews is not acceptable, and plans to reassess rate adequacy every three years.

Background

The Town has 794 utility customers with 96% of the customers being residential and small commercial accounts. The Town also provides water to some residents located in the R.M. of Glenwood (Glenwood).

Pursuant to an agreement with Glenwood, the Town charges these customers the same rates as are charged to Town residents, plus a surcharge to recover a portion of the Town's utility capital

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costs (including improvements to the water treatment plant). As well, Glenwood assesses a local improvement levy of \$145.78 annually against the Town's Glenwood utility customers, and remits the funds to the Town.

The Town has no major industrial utility customer and population growth has been stagnant. A considerable number of the Town's residents are elderly and on fixed income, and utility rates are an important issue.

The Town's water supply is a well drilled into an aquifer, utilizing reverse osmosis and green sand filtration treatment to produce blended water. The Town's water supply has been more than adequate. Capacity at the water treatment plant, north reservoir and pumphouse is 180,000, 50,000 and 130,000 gallons, respectively. The water treatment plant was last upgraded in 2003.

The Town's wastewater treatment plant (WWTP) was built in 1981 and consists of an extended aeration treatment process, two clarifiers, chlorine disinfection and de-chlorination. Sludge is trucked regularly to an offsite disposal area. No primary treatment exists, and sewage discharges are made into the Souris River.

In 2004, Wardrop Engineering reviewed the status of the WWTP and advised significant upgrading was required. Due to severe corrosion, much of the equipment required replacement with

corrosion resistant material. Certain expenditures totalling \$323,000 were required immediately, and were included in the Town's 5-year outlook for capital expenditures of \$1.9 million (10-year outlook, a further \$738,000), expressed in 2004 dollars.

The historical capital cost of the Utility system was reported to be \$5.5 Million, though replacement cost would be multiples of that. The Town's portion of the cost of the water treatment plant upgrade, after government grants, was met by a debenture, to be repaid over 10 years through tax roll assessments. Annual servicing of the debenture debt is at a cost of \$118,812.82. As noted earlier, the wastewater treatment plant is to be upgraded in phases commencing in 2007.

As of December 31, 2006, the utility had approximately \$158,000 in utility accumulated surplus and a reserve fund of approximately \$127,000. The anticipated losses for 2007 and 2008 will reduce these balances, providing further evidence of a requirement for large rate increases.

The Town indicated awareness of provincial discussions regarding nutrient removal but reported no current plans to remove phosphorus and nitrogen, as the Town has yet to be involved in discussions with the Province. The Town reported that adequate water supply has not required a water conservation information campaign, to-date.

Board Findings

The Board, in this Order, approves the revised water and sewer rates and schedules as applied for by the Town. However, given projected accumulated utility operating deficits for 2008 and 2009, the Board will direct implementation of the 2007 increase as of the July 1, 2007 billing rather than the October 1 billing as proposed by the Town.

The Board notes the unauthorized bulk water increase of 2003, whereby the bulk water rate was increased by three-fold without Board approval. By this Order, the Board approves the 2003 increased rate going-forward. The new rate is more representative of customer rate fairness, as bulk water users are not required to pay taxes to the Town and thus may not have contributed to the capital cost of the system. The Board understands that less than 2% of water sold each year is currently sold on a bulk water basis.

As this amount is not material to the overall economics or situation of the Town, the Board will refrain from action with respect to the period of an unauthorized rate, but reminds the Town that all rates are to be approved by the Board prior to being implemented or amended.

Manitoba law expects utility operating costs to be met by utility operating revenue. Deficits must be recovered either through further increased utility rates, draws from utility

surplus, reserves or on special occasions contributions from the General Fund.

Although the rate increases are very large, the Board remains concerned that the new rates, when fully implemented in 2009, will not prove adequate to fund the reported needed infrastructure renewal program.

While reserve and contingency provisions totalling approximately \$80,000 annually are provided for in the new rates, perhaps more than half of these contributions will be offset by operating losses in 2007 and 2008. Even if the losses now projected for 2007 and 2008 are not incurred to the level estimated, utility reserves will likely prove inadequate to meet the capital needs of the Town.

Further, if MWSB and senior government grants are not forthcoming in the time frame desired by the Town, identified and needed projects may have to be deferred until the grants are available or the Town's borrowing capacity increases. The Board understands the Town is close to its borrowing limit, placing further pressure on the prioritization of utility capital projects.

Regarding the provision of services beyond the Town's boundaries, the Board expects the existing surcharge to be reviewed and adjusted from time to time, to ensure a fair recovery of operating and capital costs from all customers.

And, the Board expects the local improvement levy to be revisited and possibly adjusted after the wastewater treatment plant has been upgraded.

Concerning the bulk water charge, the current bulk water rate is sufficiently above the commodity rate charged to connected residents to provide fairness to Town residents. Bulk water users are, through the rate, making a contribution to the capital costs of the system.

With respect to the differing level of sewer services provided by the Town, the Board understands that all customers pay the same sewer rate notwithstanding that there are extra costs incurred by those on the low-pressure system whom are obliged to pay for pump-out and trucking services. The Board understands that the situation arose because of the Town's borrowing capacity shortfall and topographic issues, when the customers on the low-pressure system were connected.

While accepting the Town's defence of charging all sewer customers the same billing rate despite some of the customers not being on the gravity flow (solid and liquid waste) system, the Board suggests that the Town review the matter before making its next rate application to the Board.

Environmental Issues

The Board notes that the Town has yet to be involved in provincial discussions related to nutrient removal from effluent. At some point in the future, the Town may expect to be involved in such discussions. Nutrient removal will likely involve substantial costs, and require further rate increases at some point beyond 2009.

The Town rate schedules continue to be based on declining rate blocks ("the more you use the less you pay"). While arguments have been made for declining block schedules based on the premise that fixed utility costs do not increase with higher volumes, there are problems with the approach. Declining rate block systems do not recognize the value of water to the same degree that single rate schedules do. And, declining rate block systems may encourage excess consumption.

The Town should investigate the possibility of amending its rate schedule and adopting a single rate approach for its next rate application. Such a change may prove particularly beneficial to the Town's elderly fixed-income households, while encouraging higher volume customers to conserve and reduce water use.

The Board understands that provincial standards for drinking water quality and sewage discharge safety (nutrient removal not being a current requirement for the Town) are being met.

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IT IS THEREFORE ORDERED THAT:

1. By-law No. 1820 is hereby approved, with the revised rates to be effective on all billings on and after July 1, 2007, January 1, 2008, and January 1, 2009.
2. The Town of Souris is to file a copy of the By-law with the Board after final passing.
3. The Town of Souris is to file its utility financial statements for 2007, 2008 and 2009 with the Board, with commentary on infrastructure renewal program and rate adequacy, within six months of each respective year end.

Fees payable upon this Order - \$1,250.00.

THE PUBLIC UTILITIES BOARD

"GRAHAM LANE, C.A."

Chairman

"G. GAUDREAU, CMA"
Secretary

Certified a true copy of
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Public Utilities Board

Secretary