

NOVA SCOTIA UTILITY AND REVIEW BOARD

IN THE MATTER OF THE PUBLIC UTILITIES ACT

- and -

IN THE MATTER OF THE APPLICATION of the **MUNICIPALITY OF THE COUNTY OF INVERNESS**, on behalf of its **Water Utility**, for approval of amendments to its Schedule of Rates and Charges for Water and Water Services and its Schedule of Rules and Regulations

BEFORE: John A. Morash, C.A., Member

APPEARING: **MUNICIPALITY OF THE COUNTY OF INVERNESS**

William H. Gates, MBA, P. Eng.
W. H. Gates Utility Consultants Ltd.

Kate Beaton
Chief Administrative Officer

Joe O'Connor, P.Eng.
Director of Public Works

E. A. Smith
Director of Finance

HEARING DATE: January 18, 2007

FINAL SUBMISSIONS: February 8, 2007

DECISION DATE: **March 30, 2007**

DECISION: **Schedule of Rates and Charges Approved as Amended
Schedule of Rules and Regulations Approved as Amended**

SUMMARY

[1] The Municipality of the County of Inverness (the "Municipality", the "County") applied to the Nova Scotia Utility and Review Board (the "Board") on behalf of its Water Utility (the "Utility", the "Applicant") for amendments to its Schedule of Rates and Charges and Schedule of Rules and Regulations pursuant to the *Public Utilities Act* (the "Act"), R.S.N.S. 1989, c. 380. The existing Schedule of Rates for Water and Water Services has been in effect since July 1, 2006. The existing Schedule of Rules and Regulations has been in effect since January 1, 2006. The Schedule of Rules and Regulations was amended by Board Order dated February 9, 2006 to provide for the inclusion of the Whycomomagh water system in the definition of the systems served by the Utility.

[2] The Utility serves customers within the Municipality through the five distinct water systems of Inverness, Judique, Mabou, Port Hood and Whycomomagh. A sixth system in Port Hastings is expected to be served by the Utility upon completion of the necessary infrastructure, scheduled for April 2007. The Port Hastings system is to be supplied water by the Town of Port Hawkesbury ("Town") Water Utility, which will be purchased by the Utility at the bulk water rate approved by the Board in its decision dated February 13, 2007 with respect to an application by the Port Hawkesbury Water Utility to amend its rates and charges [2007 NSUARB 11]. The estimated costs associated with serving the community of Port Hastings, beginning in 2007/08 are included in this Application.

[3] The Application proposes rate increases for its existing customers and the projected customers located in Port Hastings for the test years of 2007/08, 2008/09 and 2009/10. The proposed increases for unmetered customers, assuming annual consumption of 250 cubic metres, are 35.7%, 32.2% and 3.6%, respectively. For residential customers with a 5/8 inch meter and annual consumption of 185 cubic metres, the proposed increases are 19.3%, 33.0% and 3.7%, respectively. For all other metered customers (3/4" to 4"), the average rates are proposed to increase 17.6% to 66.7% in 2007/08, 29.3% to 39.1% in 2008/09 and 3.2% to 4.2% in 2009/10, respectively. Due to the elimination of the block consumption rate structure in 2007/08, the meter sizes with the largest average consumption, namely the 2" and 3" meters, incur the largest proposed increases of 40.1% and 66.7%, respectively.

[4] The Application further proposes increases to the annual public fire protection charge to be paid to the Utility by the Municipality of 9.5% in 2007/08, 68.1% in 2008/09 and 0.5% in 2009/10.

[5] The public hearing was held at the Port Hood Fire Hall on January 18, 2007 after due public notice. William H. Gates, MBA, P. Eng., of W. H. Gates Utility Consultants Ltd., was the Utility's consultant. The Utility was also represented by Municipal staff: Kate Beaton, Chief Administrative Officer; Joe O'Connor, Director of Public Works; and E.A. Smith, Director of Finance. The Board received three letters of opposition to the proposed amendments, as well as one inquiry with respect to the proposed unmetered rates.

[6] The Rates and Rules and Regulations, as amended, are approved.

INTRODUCTION

[7] The Applicant currently serves approximately 1250 customers, including approximately 600 unmetered customers, in the five communities of Inverness, Judique, Port Hood, Mabou and Whycocomagh. It is projected that there will be 179 new customers in 2007/08 associated with the Port Hastings system. The Utility plans to meter the majority of its customers during the period of 2007/08 to 2009/10, when it is projected that approximately 50 customers will be unmetered. The meters will primarily be installed in the Judique and Whycocomagh systems, which are currently not metered, and in the new system of Port Hastings.

[8] The Inverness water system is the largest, serving approximately 670 customers. Its source of supply is surface water, which is treated through filtration and chlorination, and two wells with treatment for iron and manganese removal and disinfection.

[9] The Judique system is a small system serving approximately 65 customers, with a surface source of supply. In 2002 a dissolved air floatation treatment unit was added to the system.

[10] The Port Hood system serves approximately 225 customers and is supplied by two wells. Treatment is provided for iron and manganese removal as well as filtration and disinfection.

[11] The Mabou system is spring fed and serves approximately 140 customers.

The water is chlorinated at the treatment plant.

[12] Approximately 150 customers are served by the Whycocomagh system. The source of supply is two deep wells. The water is chlorinated prior to entering the distribution system.

[13] The Port Hastings system, which is expected to be included in the Utility in April 2007, will obtain treated water from the Town. It is projected that in order to serve the Port Hastings system, the Utility will annually purchase 41,375 cubic metres (9,102,500 gallons) of water from the Town at the Board approved wholesale rate. A 200,000 gallon reservoir has also been constructed which will provide fire protection to the Port Hastings area. The area is currently served by individual wells and it is estimated that approximately 153 - 5/8" meter residential customers and 26 - 3/4" meter customers in Port Hastings will connect to the new system in 2007/08.

[14] In order to comply with the provisions of the Nova Scotia Department of Environment and Labour (NSEL)'s document - *A Drinking Water Strategy for Nova Scotia (Drinking Water Strategy)*, assessment reports for each of the Utility's systems were prepared in 2004. These reports identified a number of 'gaps' between the current systems' infrastructure and the requirements of the *Drinking Water Strategy*, which must be adhered to, effective April 1, 2008. The capital budget proposed, as a part of the Application, includes among other items, the estimated costs of the infrastructure improvements, totalling approximately \$2.6 million, as identified in the system assessment reports.

[15] It has been the practice of the Municipality for several years to transfer funds to the Utility to cover the Utility's operating losses. This transfer of funds is proposed to be eliminated beginning in 2007/08.

[16] The Application was presented to the Board based upon the need to increase rates as a result of the financial requirements of the Utility. In particular, the Application is based upon increased costs of maintaining the existing level of service; costs associated with the upgrade of the water treatment and distribution systems; costs of compliance with the Provincial Water Strategy; and the costs associated with the installation of the system in Port Hastings. A Rate Study to support the proposed rate increases, dated November 1, 2006, was prepared by W. H. Gates Utility Consultants Ltd. (Exhibit I-2).

RATE REVIEW

a) Operating Expenses

[17] The Rate Study projects that at current rates, with no further transfers from the Municipality, the Utility will incur operating deficits for each of 2007/08, 2008/09 and 2009/10 of \$224,375, \$430,270 and \$452,105, respectively.

[18] The operating expenses contained in the Rate Study are based upon the Utility's budget for the year 2007/08 with a projected increase of 3% in 2008/09 and 2009/10, for each of the line items, with the exception of source of supply and depreciation. The source of supply expense for the years 2007/08, 2008/09 and 2009/10 includes the cost of the projected annual amount of water to be purchased from the Town (41,375 cubic

metres), at rates approved by the Board, to supply the Port Hastings system. The annual depreciation expense is based upon the Utility's proposed capital additions.

[19] Between 2006/07 and 2007/08, the Utility's operating expenses are projected to increase from \$421,754 to \$521,505. The response to an information request (Exhibit I-3, IR-12) indicated that \$61,099 of this total increase of \$99,751 is the result of adding the Port Hastings system to the Utility. Mr. Gates explained that the increases in power and pumping and transmission and distribution included increased pumping associated with the pumping station in Port Hastings, and increased costs associated with the operation of the new distribution system in Port Hastings, respectively. He noted that the estimates are based upon the best information available.

[20] The Board questioned the reasonableness of the approximately \$40,000, or 9.4% increase in 2007/08, in the operating expenses not attributed to the Port Hastings system, given the projected 3% increase in subsequent years. Mr. Gates responded:

...this [2007/08] was a detailed budget produced by the utility and we used that - - or I used that detailed budget. And with the absence of any detailed budget for the next two years I used three percent. Had they done a detailed budget it might have been more than that. I tend to think that three percent, considering the potential of added work, could well be minimal for the last two years.

[Transcript pp. 78, 79]

Upon Board questioning, Mr. Gates confirmed that in his opinion the projected 3% increase for each of 2008/09 and 2009/10 could well be minimal.

[21] The operating expense items were examined by the Board. The collection and administration expenses increased from \$39,882 in 2004/05 to \$50,007 in 2005/06. The response to an information request (Exhibit I-3, IR-7) explained that this increase was

due to costs associated with consulting fees to review the systems and to prepare the Rate Study. These costs are carried through in the projections during the test period. Mr. Gates noted during the hearing that:

...there will be some ongoing consultants expense for the next foreseeable future to keep – trying to keep up to date with this - - with these requirements of Labour - - Environment and Labour....

[Transcript p. 72]

[22] The water treatment operating expense is proposed to increase from \$121,318 in 2006/07 to \$133,000 in 2007/08. The response to an information request explained:

Upgrades to the treatment plants have resulted in an increase in maintenance and operating costs.

[Exhibit I-3, IR-11b]

None of the proposed increase in water treatment expense is attributed to the Port Hastings system.

[23] The response to an information request described the Utility's budgeting process:

The Director of Public [w]orks and the Director of Finance prepare a draft budget for the utility's operation. This draft budget is reviewed with the CAO and revisions made as required. The budget for the next financial year is approved by County Council.

[Exhibit I-3, IR-17]

The budgeting process was further discussed during the hearing. In response to the Board's question as to whether this process was followed in the determination of the budgeted operating expenses in 2007/08, Ms. Beaton stated:

Yes. We looked at the different operational components of the utility and we were satisfied that those figures were a fair estimate of what our operating costs were going to be.

[Transcript pp. 80,81]

In response to Undertaking, U-1, the Utility provided a further explanation for the budgeted increases for each of the operating expense items in 2007/08.

[24] As a result of the Board's decision, dated February 13, 2007, with respect to the Port Hawkesbury Water Utility's rate application, the wholesale rate for the sale of water to the Utility to supply Port Hastings has decreased slightly from that proposed in this rate application. This has the effect of reducing the source of supply costs. Based upon the projected quantity of water sold, this results in a decrease in the projected source of supply costs contained in this Application by \$555, \$572 and \$1,678 for each of 2007/08, 2008/09 and 2009/10, respectively.

[25] The response to an information request (Exhibit I-3, IR-22b) indicated that the proposed capital addition of meters in the amount of \$30,000 in 2009/10 should have been depreciated at a rate of 5%, in accordance with the *Accounting and Reporting Handbook for Water Utilities* ("*Accounting Handbook*"), and not the 2% used. The Board has corrected this, which results in additional annual depreciation of \$900. This amendment affects annual depreciation beginning in 2010/11, which is beyond the Application's test period, and therefore has no effect on rates.

[26] It was noted during the Utility's last rate application in 2005 that the Utility has in some cases been using lower depreciation rates than the rates specified in the *Accounting Handbook*, resulting in a lower annual depreciation expense. Given the significant rate increases proposed at that time, and the Board's review of the *Accounting Handbook*, the depreciation rates used were deemed acceptable. For the same reasons,

the Board accepts the current depreciation rates used in this Application, with the exception of metering in 2009/10 noted above. However, the Board again reminds the Utility that it should review its depreciation rates after the issue of the revised *Accounting Handbook*, and make any necessary adjustments to its depreciation rates.

[27] The Board has considered the remainder of the Utility's projected operating expenses. The Board understands that there will be ongoing expenses with respect to complying with NSEL Regulations and accepts the Utility's collection and administration expenses over the test period as reasonable.

[28] It is further understood that additional expenses for power and pumping will be incurred in 2007/08 which are associated with the addition of the Port Hastings system and that these expenses are based upon the best estimates available at the time. The Board accepts the Rate Study's projected power and pumping expenses for the test period.

[29] With respect to the water treatment costs, it is reasonable to expect increases in water treatment costs associated with the upgrades in the plants contained in the proposed capital budgets. The Board considers that the projected water treatment expenses are reasonable in the circumstances.

[30] The Board has also considered the projected transmission and distribution expenses for the years 2007/08, 2008/09, and 2009/10. This item was discussed at length with Mr. Gates during the hearing. A major component of transmission and distribution is the watermain breaks which occur from time to time. Mr. Gates indicated that a major break could cost \$15,000 to repair.

[31] The Board notes that in the year 2004/05, the actual transmission and distribution expense was \$151,414. For the year 2007/08, the Utility has budgeted \$156,000 and increasing 3% per year in the next two years.

[32] Upon reviewing the evidence of Mr. Gates and Ms. Beaton, the Board is satisfied that the projected expenses for the test periods were reviewed carefully by the Utility, and the Board accepts the projected transmission and distribution expenses as reasonable.

b) Proposed Capital Budget and Funding

[33] Included in the Rate Study is the Utility's proposed capital budget for 2006/07, 2007/08, 2008/09 and 2009/10 totalling \$470,000, \$2,185,105, \$180,880 and \$90,000, respectively. The majority of the projects contained in the capital budgets relate to infrastructure upgrades necessary to comply with NSEL Regulations. Meters in the amounts of \$70,000, \$120,000 and \$30,000 are included in the budget for 2006/07, 2007/08 and 2009/10, respectively. The installation of meters was not a requirement of NSEL. The rationale for metering was discussed during the hearing:

Mr. Gates: Well, there has always been a desire on the part of the utility that more customers should be metered. And they made a conscious decision with the support of the council of the municipality to really work hard to meter all the customers, which is the right thing to do, and - - because they had gone for years in some cases with no meters at all. I mean, some places in Inverness have never been metered. And they are now at a conscious effort to make sure that everyone is metered that can be metered over the next three years.

The Chair: And the water consumption is - - for unmetered, presumably, is significantly higher than the metered.

Mr. Gates: That is correct. Now that - - practically all the water supply in this utility, other than the water that's purchased from Port Hawkesbury, is treated. And treatment is getting more expensive every year. So as a result it makes sense to have everybody metered so that they pay their fair share.

[Transcript p. 39]

[34] Upon Board questioning with respect to the necessity of the capital projects contained in the Rate Study, Mr. O'Connor confirmed that, based upon the conclusions of the system assessment reports, the Utility must complete the projects to comply with NSEL Regulations. Given the significant infrastructure upgrades proposed, in particular in 2007/08, the Board questioned whether any of the projects could be delayed in order to reduce the impact on rates. Mr. Gates explained:

Well, the sort of drop-dead date from Department of Environment is April 1st, 2008. So they want their deficiencies as much as possible completed and brought up to scratch by April the 1st, 2008.

[Transcript p. 54]

[35] With respect to the issue of whether it is reasonable to project that the Utility could complete \$2 million in capital works over a number of systems in one year, Mr. Gates noted that a consulting engineer could handle the work. He added that although there may be areas which will not be completely finished, it is his opinion that most of the \$2 million will be needed in 2007/08.

[36] During the hearing, the Board questioned the process used to determine the estimated capital project costs contained in the Application. Mr. O'Connor explained:

There were actually no estimates in the assessment reports. They basically identified gaps in the system and then we looked at how we were going to rectify those gaps that were in the systems. And so there was sort of ongoing work to come up with estimates on how we were going to do that and what was required...

[Transcript p. 83]

He added that the Utility obtained costing information on the projects identified in the system assessment reports from consulting engineers, C. J. MacLellan Ltd. The Utility provided supporting information for the capital budgets for each of the test years in response to Undertaking, U-2. The Undertaking response noted:

The attached pages from the C.J. MacLellan report formed the bases [sic] of the cost estimates. As the estimates were dated the Director of Public Works revised the estimates as set out in Sheet 1. These estimates were used to develop the Capital budget in Schedule 4 [of the Rate Study].

[February 8, 2007 letter attached to Undertaking, U-2]

[37] The proposed funding for the capital projects consists of capital out of revenue in the amount of \$25,000 for each of the test years; withdrawal from the depreciation fund of \$245,000, \$58,105, \$155,000 and \$65,000 for each of 2006/07, 2007/08, 2008/09 and 2009/10; external funding of \$200,000 in 2006/07 and long-term borrowing of \$2,102,000 in 2007/08, assumed to be repaid at 6% over 20 years.

[38] The response to an information request (Exhibit I-3, IR-19) indicated that the Utility's current depreciation fund balance is \$269,406 which, along with the projected annual depreciation expense is sufficient for the proposed funding. A revised capital fund balance sheet filed in response to Undertaking U-3 shows a depreciation fund balance of \$34,897 at the end of the test period, based upon the assumptions of the Rate Study.

[39] The rationale for the proposed funding as capital out of revenue for each of the test years was explained:

In the test years and in future years there will continue to be ongoing capital projects such as Main replacements and water meters. The utility considers it prudent that some of this capital expense should be from current revenue to reduce borrowing. If the total cost of capital projects exceeds the estimate, some of the capital out of revenue could be used for debt financing.

[Exhibit I-3, IR-16]

[40] Ms. Beaton explained that the Utility had submitted an application to the Municipal Rural Infrastructure Program for external funding for the \$2.6 million in capital upgrades identified in the system assessment reports. She noted that although the application was not denied, approval was not received, and that in the interim period, funding in the amount of \$200,000, as indicated in the Rate Study for 2006/07, was provided under the Provincial Capital Assistance Program. When questioned as to whether any additional external funding will be received, Ms. Beaton replied:

There is a continuous contact with the province on that. But there is no infrastructure money available, and the response to us is that until more funding is available under that program the application is not being considered.

[Transcript p. 92]

She confirmed that based upon the current information available, it appears that no further external funding for the \$2.6 million in capital upgrades will be received. Mr. O'Connor added that it is his opinion that small amounts of funding, similar to the \$200,000 may become available, but nothing more substantial.

[41] The Board noted the substantial rate increases proposed in 2008/09, the first year that the principal and interest payments associated with the long-term borrowing of \$2,102,000 in 2007/08 occur. The projected rate increases in 2009/10 are significantly less than those in 2008/09 and the Utility was questioned as to whether it considered spreading out the rate increases over a couple of years. Mr. Gates responded:

...the only alternative to reduce the second year would be if you short term some of it [the long term debt] so that you're not paying any principal, you're only paying interest, bank interest, and then borrow more the following year. That is one possibility.

[Transcript p. 59]

He noted that this would reduce the revenue requirement in 2008/09 by approximately \$60,000, the amount of the principal payment. He added that "...if the rates were going... in the \$100 range you should really look hard at that." (Transcript p. 62). However he noted that a comparison indicates that the proposed rates are lower than many other utilities with recent rate increases, including the Town.

[42] In a letter to the Board dated February 7, 2007, Mr. Gates provided further comments concerning the matter of deferring the issue of long-term debt by one year in order to 'smooth out' the rate impact. The letter notes:

I have reviewed with Ms. Beaton the possibility if [sic] deferring the issuing of \$2,102,000 of debt for one year and only incurring the interest cost on the debt in 08/09.

The Utility is prepared to defer the issuing of the debt for one year with the resulting savings in principal payments of \$57,132 in 08/09.

[February 7, 2007 letter from W. H. Gates Utility Consultants Ltd.]

Attached to the letter was a Schedule which showed the effect of the deferral which moves towards more evenly spreading the increases over the test period.

[43] The Board has considered the Utility's proposed capital budget. Based upon the information presented during the hearing it is the Board's understanding that the proposed infrastructure upgrades are necessary for compliance with Provincial Regulations. The Board has reviewed the estimated costs of the projects, which are based upon estimates prepared by consulting engineers in 2005, as submitted in response to Undertaking U-2. The estimates have been updated by the Utility to reflect inflationary effects. After reviewing the estimated costs in Undertaking U-2, the Board accepts the capital budgets as presented in the Rate Study. The Utility is reminded that the inclusion

of the proposed capital projects in the Rate Study does not constitute the Board's approval of these projects. Separate Board approval is required for projects in excess of \$25,000 as set out in s. 35 of the *Act*. The Board notes that the Utility has received approval for the 2006/07 projects contained in the Rate Study.

[44] With respect to the proposed funding of the capital budgets, the Board finds the Utility's source of funding from depreciation to be reasonable. The Board has also considered whether or not the annual \$25,000 capital from revenue charge for the years 2007/08, 2008/09 and 2009/10 can be funded from the depreciation fund rather than from operations. Based on the information filed, there does not appear to be a sufficient balance in the Utility's depreciation fund to eliminate all of the proposed capital out of revenue and replace it with funding from depreciation for each of the three test years. However, one of the three years could be accommodated out of the depreciation fund. Therefore, the \$25,000 capital out of revenue in 2008/09 has been removed and replaced with funding from depreciation, with the remaining capital out of revenue accepted as proposed. This will have a further effect of spreading out the percentage rate increases.

[45] The Board has considered the information presented during the hearing, as well as the supplemental information filed by Mr. Gates with respect to deferring the issuance of long-term debt for one year. This will result in the Utility treating the funds required in 2008/09 as short-term financing with no principal payment required in 2008/09. In the year 2009/10 this loan will be structured as a long-term loan, requiring interest and principal payments. It appears that this change is acceptable to the Utility, as noted in the

February 7, 2007 letter to the Board. Given that the effect of this amendment is to reduce the significant percentage increase proposed in 2008/09, the Board accepts this deferral and has reduced the revenue requirement in 2008/09 by the principal payment on the loan of \$2,102,000.

c) Non-Operating Revenue and Expenditures

[46] Included in the Rate Study's revenue requirements are projections over the test period of non-operating expenditures for interest on operating overdraft in 2007/08, repayment on the new debt of \$2,102,000, and annual capital out of revenue of \$25,000. Non-operating revenue, associated with the interest on cash balances is estimated to be \$5,775 in 2006/07 and is increased annually by 3% for each of the test years.

[47] The interest on operating overdraft is explained in the Rate Study:

In 07/08 the required borrowing of \$2,102,000 (Schedule 4) will be short term for one half year at a rate of 3% (borrowing from the County's general fund). The short term loan will be converted to long term debt in 08/09 with interest and principal as calculated in Appendix 1 [of the Rate Study].

[Exhibit I-2, Notes on Schedules]

During the hearing, the Board questioned whether the short-term interest is related to construction and should be capitalized. Mr. Gates explained:

No. It's assumed by the end of 07/08, that two million one hundred thousand will be spent, of which they've got a short term that two million one for half a year until they start to - - until they get the borrowing in the following year.

[Transcript p. 68]

[48] On March 28, 2007, Mr. Gates sent a letter to the Board in which he indicated that the short-term interest of \$31,530 in the test year 2007/08 could be capitalized. The

Board understands that this short-term interest is related to the construction-in-progress and accordingly, the Board believes that it should be capitalized. The related depreciation expense for the test years 2008/09 and 2009/10 has not been adjusted for this, as it was considered to be relatively immaterial.

[49] The Board has considered whether the short-term interest of \$31,530 in the test year 2007/08 should be deleted as a non-operating expenditure in view of the fact that it is to be capitalized, as set out above.

[50] In this rate application, as in many other similar applications for the smaller utilities, the revenue requirement is determined on a “cash sufficiency” basis. This means that the revenues can only be determined after the operating and non-operating expenditures are determined. In other words, the revenues will be set at an amount which provides the utility with sufficient funds to enable it to pay for all its expenditures. If a non-operating expenditure is not included in a test year, then the utility will not be able to recover the cost of that expenditure through the rate structure. For example, if a utility’s capital project is funded through a long-term debt issue, the costs to the utility for that project are reflected in the monthly debt charges the utility must pay on the long-term debt. These debt charges consist of both interest and principal payments. If these payments are not reflected in the test year expenditures as part of the rate determination process, then the expenditures will not be included in the rates, and the utility cannot generate sufficient funds to pay for the cost of the capital project.

[51] The situation is the same for interest during construction. The only difference

between interest incurred during a period of construction and the interest referred to in the above paragraph is that the interest incurred during construction also has to be capitalized and shown as a fixed asset in the capital fund balance sheet. However, it is at the same time a non-operating expenditure, the cost of which the utility must recover from the rate structure. It is, in essence, part of the revenue requirement.

[52] In addition to the short-term interest in 2007/08, the Rate Study projects expenses during the test period, related to the new debt, of \$57,132 and \$60,580 in principal payments in 2008/09 and 2009/10, respectively, and interest payments of \$126,120 and \$122,694, respectively.

[53] As discussed above, the Board has amended the Rate Study with respect to the long-term debt which results in the elimination of the principal payment in 2008/09. The Board has further eliminated the capital out of revenue amount of \$25,000 in 2008/09 as discussed above. The Board accepts the non-operating revenue as proposed in the Rate Study.

[54] An amendment to the Application's calculated return on rate base was filed in response to an information request (IR-32, Exhibit I-3), which indicates a return on rate base, based upon the assumptions of the Rate Study, of 1.01%, 4.03% and 4.03% for each of 2007/08, 2008/09 and 2009/10, respectively. The amendments to the non-operating expenses in 2008/09, the elimination of the capital from revenue in 2008/09 and the elimination of the principal debt payment in 2008/09, result in a reduction of the return on rate base for that year to 2.38%. The return on rate base for the other two test years are as contained in the Rate Study. The Board approves the Utility's return on rate base

for 2007/08, 2008/09 and 2009/10 of 1.01%, 2.38% and 4.03%, respectively.

d) Allocations of the Revenue Requirement

i) Fire Protection

[55] The methodology used in the determination of the public fire protection charges is generally consistent with that used in recent rate studies approved by the Board. The allocation of utility plant in service to fire protection, based upon the proposed capital additions, is 33.9% in 2006/07, 37.2% in 2007/08 and 36.3% in 2008/09.

[56] Based upon the assumptions of the Rate Study, the annual fire protection charge to the Municipality, which was \$109,309 in 2005/06, is proposed to increase to \$119,747 in 2007/08, \$201,257 in 2008/09 and \$202,342 in 2009/10.

[57] The Board finds that the methodology used to determine the annual fire protection charge to the Municipality is reasonable. However, the revision to the source of supply expense as a result of the reduction of the wholesale rate, the elimination of the capital out of revenue in 2008/09 and the deferral of the issue of long-term debt, all have the effect of reducing the proposed fire protection charges. In addition, as the amendments have the greatest effect on the revenue requirement for 2008/09, the greatest reduction in fire protection rates from that proposed is in 2008/09. The proposed fire protection rates consisted of an increase of 68.1% in 2008/09, followed by a minimal increase of 0.54% in 2009/10. The revisions have the effect of spreading out the percentage rate increases to the fire protection charge, which results in an increase of 42.6% in 2008/09 and 18.4% in 2009/10.

[58] The Board accepts and approves the fire protection charges to the Municipality, based upon the amendments described above.

ii) Water Utility's Customers

[59] The remaining revenue requirement after the allocation to fire protection is to be recovered from the Utility's customers. The allocation of the operating expense items to the various categories under revenue required from metered service is generally consistent with the methodology used in other recent water rate studies. The response to an information request (Exhibit I-3, IR-33a) explained the allocation of transmission and distribution expense at 50% to base charge and 50% to delivery in order to have a better relationship between base and consumption charges. The allocation of return on rate base at 40% to base and 60% to production was explained:

The highest amount of capital spending is for water treatment upgrades and is production related. Return on rate base, which is mostly borrowing costs, was therefore allocated 60% to production. As the utility is requesting a commodity rate, it would not have any effect on the rates if some of the return on rate base was allocated to delivery.

[Exhibit I-3, IR-33b]

[60] Although the Utility has initiated a metering program, the Rate Study projects that there will be 48 unmetered customers at the end of the test period. Mr. Gates explained that the figure is an estimate as there are some customers who cannot be metered due to problems with freezing. The rates for the unmetered customers are based upon the proposed base charges for the 5/8" residential customers, and the proposed consumption charges applied to an annual consumption of 250 cubic metres. The Applicant explained why the estimated annual consumption for unmetered customers had

increased from approximately 208 cubic metres used in the last Application in 2005:

The estimated amount of water used by unmetered customers of 208 cubic metres in the last study was too low resulting in unmetered customers not wanting to be metered. The 250 cubic metres is closer to the normal estimate for unmetered customers in other utilities.

[Exhibit I-3, IR-40]

When questioned by the Board, Mr. Gates explained that in his opinion the 250 cubic metres is not unreasonable.

[61] Mr. Gates stated that in his opinion the proposed rates are just and reasonable. It was further the opinion of each of the Utility representatives that the proposed rates are just and reasonable.

[62] The Board accepts the methodology used in the allocation of the various expense items to the base, customer, delivery and production categories. The Board further accepts the calculation of the unmetered rate, based upon the annual consumption of 250 cubic meters. The revisions discussed above with respect to the elimination of \$25,000 in capital out of revenue in 2008/09 and the deferral of issuing long-term debt to 2009/10 reduces the rates to be applied to the Utility's customers, in particular in 2008/09, and has the effect of spreading out the increases. For example, in the years 2007/08, 2008/09 and 2009/10, it is proposed in the Application that an average 5/8" residential customer will have a quarterly water bill of \$56.31, \$74.86 and \$77.60, which represents increases of 19.3%, 33.0% and 3.7%, respectively. The amendments discussed above result in a quarterly water bill for an average 5/8" residential customer of \$56.25, \$68.05 and \$77.42, which represents increases of 19.1%, 21.0% and 13.8%, respectively for the same years.

e) Other Rates and Charges

[63] The Application proposes one change to the other charges contained in its Schedule of Rates. The charge for non-negotiable cheques is proposed to decrease from \$15 to \$10. Mr. Gates explained that the change is proposed in order to be consistent with the amount charged by the Municipality. No changes are proposed to the Utility's other miscellaneous charges for items such as sprinkler service, private hydrants, re-establishing water service, connection and missed appointments which were updated during the last rate application in 2005.

SUBMISSIONS

[64] Patricia Gibson, a customer of the Utility residing in Judique, spoke during the hearing. She noted that there are a number of seniors supplied water by the Judique water system, who generally use less water than large families, and requested that the Utility have a discount rate for seniors.

[65] The Board received three letters from Utility customers of the Whycocomagh system in opposition to the proposed rates. The letters commented on the significant increases proposed and the financial effect that the rates could have on seniors and those on fixed incomes.

[66] Prior to the hearing, Board staff spoke with a Utility customer in Inverness who questioned the proposed rate increases for unmetered customers. Mr. O'Connor

noted during the hearing that he spoke with the customer after his conversation with Board staff, and it was Mr. O'Connor's opinion that the matter has been resolved.

[67] The Board has considered the information presented by Utility customers. With respect to the issue of a specific rate for service to seniors, the Board notes that water rates in the Province are generally composed of a base charge, which is meter specific, and a consumption charge. There is no further distinction among the types of customers who have a particular meter size. This concept is set out in the Act, which states:

Equal rates and charges for similar services

67 (1) All tolls, rates and charges shall always, under substantially similar circumstances and conditions in respect of service of the same description, be charged equally to all persons and at the same rate, and the Board may by regulation declare what shall constitute substantially similar circumstances and conditions.

The situation described by Ms. Gibson, where an individual who uses very little water is charged the same rate for water as a family of several people, who most likely consume greater amounts of water, should be resolved through metering. As noted above, meters are projected to be installed where possible throughout the Utility, including Judique, during the period of 2007/08 to 2009/10.

[68] The Board understands the concerns of the customers with respect to the proposed rate increases. However the Utility requires major infrastructure upgrades, the costs of which must be recovered from customers. The amendments made by the Board with respect to the elimination of capital out of revenue in 2008/09 and the one year deferral of the principal payments associated with the issuing of long-term debt will have the effect of "smoothing" out the rate increases over the three year period. The Board

further notes that the proposed rates are lower than many utilities in the Province which have recently amended rates.

SCHEDULE OF RATES AND CHARGES

[69] The Board has approved the Schedule of Rates and Charges, with the amendment to source of supply expenses, the one year deferral of the long-term debt and the elimination of capital out of revenue for 2008/09, as discussed above, for water supplied on and after April 1, 2007, April 1, 2008, and April 1, 2009. The approved rates are attached hereto as Schedules "A" , "B" and "C". The detailed calculations supporting the approved rates are set out in Attachment 1 (Schedules 1 to 13).

SCHEDULE OF RULES AND REGULATIONS

[70] The only amendment to the Utility's current Schedule of Rules and Regulations proposed in the Application is to add the water system of Port Hastings to the definition of "Utility". The Rate Study is based upon the assumption that the Port Hastings system will be included in the Utility in 2007/08, and the Board has approved the wholesale rate to be applied by the Town for the sale of water to the Utility to supply the Port Hastings system. Accordingly, the Board has approved the amended definition which reads as follows:

"Utility" means the Water Utility of the Municipality of the County of Inverness as operated by the Engineering and Works Department of the Municipality, which includes the water systems of Inverness, Judique, Mabou, Port Hood, Whycomagh and Port Hastings.

[71] The approved Schedule of Rules and Regulations, with the amendment noted above, is attached hereto as Schedule "D" and is effective April 1, 2007.

[72] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, this 30th day of March, 2007.

John A. Morash

ATTACHMENT 1 IS NOT AVAILABLE ELECTRONICALLY. IF YOU WISH TO RECEIVE A HARD COPY, PLEASE CONTACT THE BOARD.

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Attachment - 1

Revised Schedules 1 - 13