

NOVA SCOTIA UTILITY AND REVIEW BOARD

IN THE MATTER OF THE PUBLIC UTILITIES ACT

- and -

IN THE MATTER OF AN APPLICATION by the **KENTVILLE WATER COMMISSION**
for approval of Amendments to its Schedule of Rates and Charges for Water and Water
Services and its Schedule of Rules and Regulations

BEFORE: Peter W. Gurnham, Q.C., Chair

APPEARING: **TOWN OF KENTVILLE**

Gerry A. Isenor, P.Eng.
G.A. Isenor Consulting Limited

Mark Phillips
Chief Administrative Officer

Fred Whynot, P.Eng.
Director of Engineering and Works

Debra Crowell, CMM, CLGA
Director of Finance

HEARING DATE: February 26, 2014

FINAL SUBMISSIONS: February 27, 2014

DECISION DATE: **April 10, 2014**

DECISION: **Schedule of Rates and Charges approved, as amended.
Schedule of Rules and Regulations approved, as
amended.**

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I SUMMARY

[1] The Kentville Water Commission (“Commission” or “Utility”) applied to the Nova Scotia Utility and Review Board (“Board”) for amendments to its Schedule of Rates and Charges for Water and Water Services and its Schedule of Rules and Regulations (“Application”) pursuant to the *Public Utilities Act*, R.S.N.S. 1989, c.380, as amended (“Act”). The existing Schedule of Rates for Water and Water Services and Schedule of Rules and Regulations have been in effect since April 1, 2012 and April 1, 2010, respectively.

[2] A Rate Study to support the Application, dated November 18, 2013 was prepared by G.A. Isenor Consulting Limited in association with Blaine S. Rooney Consulting Limited and was submitted to the Board on December 18, 2013. The Board issued Information Requests (“IRs”) with respect to the Application on January 17, 2014, to which responses were filed with the Board on January 30, 2014.

[3] The Application proposed increases in rates for the Utility customers in each of 2014/15, 2015/16 and 2016/17 (“Test Years”). A revised Rate Study was filed as a part of the IR responses which included corrections to: the annual depreciation expense; the allocation of utility plant in service to public fire protection; and the calculation of return on rate base. The revisions had a minimal impact on the rates proposed in the Application.

[4] For the 5/8” metered, residential customers, the proposed average increases in the Application are: 5.0% in 2014/15; 2.4% in 2015/16; and 1.1% in 2016/17. For all other metered customers (i.e., meter sizes ranging from 3/4” to 10”, excluding 6”), based upon the average quarterly consumption of each meter size, the

proposed amendments are between -4.5% to 12.3%, -0.3% to 6.4% and 0.9% to 3.3%, respectively in each of the Test Years.

[5] The proposed amendments to the annual public fire protection charge are a reduction of 10.4% in 2014/15, followed by increases of 4.8% in 2015/16 and 1.7% in 2015/16. The annual public fire protection charge is paid to the Utility by the Town of Kentville (“Town”) and the Municipality of the County of Kings (“Municipality” or “County”) in proportion to the number of hydrants serving each municipal unit.

[6] The public hearing was held at the Town’s Council Chambers on February 26, 2014, after due public notice. Gerry Isenor, P.Eng., of G.A. Isenor Consulting Limited represented the Utility. The Utility was also represented by Mark Phillips, Chief Administrative Officer of the Town; Fred Whynot, P.Eng., the Town’s Director of Engineering and Works; and Debra Crowell, CMM, CLGA, the Town’s Director of Finance. No members of the public spoke during the hearing.

[7] At the commencement of the hearing, Mr. Isenor explained that the Application did not include donated assets in the amount of \$2.36 million with respect to a water service extension project to the Municipality (Balsor/Eaglecrest Subdivisions). The project includes transmission and distribution mains, hydrants and services, funded by the Municipality to be turned over to the Utility at no cost. These assets were included in the Commission’s last rate application in 2010, with the anticipated transfer during the 2009/10 fiscal year. The Board approved the Utility’s request to extend service to the area served by the project in a letter to the Utility dated May 15, 2008. Mr. Whynot confirmed that there are no deficiencies in the system which would delay the takeover of the assets by the Commission. Mr. Isenor added that the Utility is

currently serving the customers associated with the extension, and that they are included in the Rate Study calculations.

[8] To correct the omission of the \$2.36 million in donated assets the Utility re-filed, following the hearing, the Rate Study as Undertaking U-1. Mr. Isenor noted that in addition to the utility plant in service, the inclusion of this project would add approximately \$36,000 in annual depreciation expense to the Test Years. He further confirmed that the response to Undertaking U-1 is to include a request, under s. 35 of the *Act*, to acquire the assets.

[9] The Rate Study as contained in the response to the IRs, which made minor corrections to the Application, was presented at the public hearing. However, during the presentation, Mr. Isenor discussed changes which would be made with the filing of the revised Rate Study in response to Undertaking U-1, noting that there would be very little rate impact on the residential rates from those proposed in the Application.

[10] The discussion in this Decision is related to the Rate Study filed in response to the IRs unless otherwise noted.

[11] The Schedule of Rates and Charges and the Schedule of Rules and Regulations are approved, as amended.

II INTRODUCTION

[12] The Utility's source of supply is groundwater from seven wells. The source water is pumped to two above ground storage facilities and flows by gravity to two other above ground storage facilities, and is then distributed to the Utility's customers. Prior to entering the storage facilities, the water is treated with the addition of sodium hypochlorite 12%, hydrofluosilicic acid and sodium hydroxide (caustic soda).

[13] The Utility confirmed that it is currently operating in compliance with Nova Scotia Environment (“NSE”) regulations. It further noted that it has received very few water quality complaints since the last rate application, and that those received generally relate to issues surrounding main breaks, such as the presence of air or sediment in the water mains.

[14] The Utility’s last rate application included estimated costs of \$1.2 million associated with a reservoir replacement project which, at the time, had some uncertainty about the funding source. The Utility confirmed that this project was completed under budget at a cost of approximately \$851,000.

[15] The Utility currently serves 3,097 customers, all of which are metered. The Application projects growth of ten residential customers annually over the Test Years, and one, 1.5” meter customer in 2015/16.

[16] The Application was presented to the Board based upon the Utility’s need to meet its present financial requirements, and to provide funds for increased operating costs and necessary capital improvements.

III REVENUE REQUIREMENTS

1. Operating Expenses

[17] For the year ended March 31, 2013, the Utility had an excess of revenues over expenditures of \$21,252 and an accumulated operating surplus of \$79,854. Based upon the assumptions of the Rate Study, with the correction to the depreciation expense as set out in the IR response, without a rate increase, the Utility is projected to operate in a deficit position in the final two Test Years, resulting in an accumulated operating deficit of \$15,488 by 2016/17.

[18] The Utility provided a description of its budgeting process in response to the IRs, noting that generally 3% is added to expenses for future years' projections, except in cases where specific figures are known. It further explained how common costs are allocated between the Town and the Utility, with 33% of the engineering and public works expenses allocated to the Utility, and two Utility employee salaries reallocated among the Utility's general ledger expenses. Ms. Crowell commented that the allocations are reviewed periodically, with the last time being three years ago. She added that she is satisfied that the allocations in the Application are accurate.

[19] The Application noted that the projected expenditures in the Test Years are based upon information provided by the Commission, with the projected expenses in 2016/17 based upon the 2015/16 figures plus 3% for inflation. Mr. Isenor reviewed the operating expense projections contained in the Rate Study, noting that most of the projected increase relates to salary adjustments and increased maintenance costs due to aging infrastructure and equipment.

[20] The source of supply expense decreases slightly in 2014/15 from 2013/14 due to maintenance on intakes and other structures associated with the well system which is not expected to reoccur. The power and pumping costs are projected to increase annually by 3% over the Test Years.

[21] Mr. Isenor noted that utility systems served by wells, such as this system, generally have much lower water treatment costs than other areas. He explained that the chemical cost, which is the largest component of the water treatment cost, is difficult to predict as it is related to both the petrochemical and the electricity industries, which he described as having price volatility. Each of the water treatment expense items is

projected to increase annually in the 2% to 9% range, for projected overall increases of 4.2%, 4.0% and 3%, respectively over each of the Test Years.

[22] The transmission and distribution expense is projected to increase by 5.9% and 5.4%, in each of 2014/15 and 2015/16, respectively. Mr. Isenor noted that these increases are primarily due to the maintenance of the distribution mains, some of which are in excess of 100 years old. The Utility confirmed that it continues to conduct annual leak detection tests, as was described during the last rate application, at an annual cost of \$5,000 to \$6,000. These amounts are included in the projected transmission and distribution expenses.

[23] The administration and general expense spiked in 2013/14, but is projected to decrease 5.5% in 2014/15, followed by increases of 2.0% and 3.0% in each of 2015/16 and 2016/17, respectively. Mr. Isenor explained the "spike" in the 2013/14 expense was due to both the included lump sum cost of the Rate Study preparation and accrued sick leave. The accrued sick leave expense was \$8,000 in 2013/14 and is projected to be \$1,100 in 2014/15. Ms. Crowell explained that the Commission's sick leave policy entitles employees to a payout at the time of leaving its employment, dependent upon the number of years worked. It is 25% at five years and 50% at ten years. There was a 'bump' in the 2013/14 year as an employee moved from the 25% to 50% level, resulting in all of the current employees at the maximum level. Ms. Crowell confirmed that as the Utility has a small number of employees, a change in categories will have a large impact on this expense.

[24] The depreciation rates for the proposed asset additions indicated in the Application are as set out in the Board's *Water Utility Accounting and Reporting*

Handbook (“*Accounting Handbook*”), with the exception of the distribution reservoirs and the repairs to the existing reservoirs items, both of which are capital projects in 2013/14. The Utility explained that the 2% depreciation rate used for distribution reservoirs was in error and should have been based upon a 75 year useful life (1.3% annual depreciation), as set out in the *Accounting Handbook*. For the repairs to the existing reservoir item, which is not specifically identified in the *Accounting Handbook*, the Utility noted that the 4% used was in error and should have been 2%. The revised Rate Study filed in the IR responses includes the corrections.

[25] The response to Undertaking U-1 further impacts the depreciation expense. Approximately \$33,000 in annual depreciation expense is associated with the assets included in the \$2.36 million projected to be transferred to the Utility in 2014/15.

[26] The Board noted that the Utility’s depreciation fund balance is not included in its financial statement’s Capital Fund Statement of Financial Position. Ms. Crowell responded that it was her understanding that the current practice deviates from that set out in the *Accounting Handbook*, and that it will be amended in the future to meet the Board’s requirements.

Findings

[27] The Board accepts the Utility’s explanation of its budgeting process as well as the allocation of costs between the Town and the Utility. The Board reminds the Utility to review the allocations in a timely manner to ensure that the Utility is recovering a reasonable share of the costs.

[28] The Board notes that projected expenses include the increased costs of maintenance of the Utility’s aging infrastructure. The Board is pleased that the Utility

has continued its leak detection program to aid in the reduction of non-revenue water. This will aid in ensuring that the Utility's variable costs, in particular chemical expense, will be used in supplying water to customers and not lost in leakage.

[29] Based upon the information provided, the Board accepts the operating expenses, including the accrued sick leave expense, as contained in the Rate Study.

[30] The Board accepts the depreciation expenses as revised in the response to Undertaking U-1, which includes both the corrections to the depreciation expense noted in the IR responses and the additional depreciation expense associated with the inclusion of the \$2.36 million of donated assets in 2014/15. These changes result in an increase in the annual depreciation expense of approximately \$27,000 over those indicated in the Test Years in the original Application.

[31] As discussed during the hearing, the Board expects that in the future, the Utility's financial statements will be prepared in accordance with the *Accounting Handbook*.

2. Capital Budget

[32] The Rate Study includes the Utility capital additions in 2013/14 totaling \$1,373,300, which includes, in addition to a number of smaller items: distribution reservoir (\$832,900); distribution mains (\$398,400); and repairs to existing reservoirs (\$66,000). Mr. Isenor explained that the reservoir is the same project which was scheduled to be built as a part of the last rate application at a cost of \$1.2 million, noting that it is the only project in the Application which requires debt funding.

[33] For 2014/15, the Application projects infrastructure additions of \$325,000. With the inclusion of the donated assets, as set out in the response to Undertaking U-1,

the capital additions are \$2,684,206. For the final two Test Years, the Utility's proposed infrastructure additions are \$390,000 and \$345,000, respectively. The proposed capital expenditures include distribution mains (not associated with the \$2.36 million donated assets) of \$225,000, \$290,000 and \$295,000, respectively in each of the Test Years. The Utility explained that these expenditures are related to the renewal of cast iron mains with a high frequency of breaks, discovered through repairs and leak detection.

[34] The Utility proposed to fund the capital expenditures in the Test Years as follows:

	2014/15	2015/16	2016/17
Water Capital Reserve	\$ 35,000	\$ 50,000	\$ 50,000
Depreciation Funds	255,000	290,000	245,000
Capital out of Revenue	35,000	50,000	50,000
	<u>325,000</u>	<u>390,000</u>	<u>\$345,000</u>
Transfer from Municipality	<u>2,359,206</u>		
	<u>2,684,206</u>		

[35] Mr. Isenor explained that the Utility attempts to do annual renewal work, in the order of \$250,000, by funding through its depreciation fund and capital from revenue in order to avoid incurring additional debt. He added that it is hoped that there will be external funding made available, through the new Build Canada Fund, which will allow them to double their infrastructure renewal efforts.

[36] The Utility noted the Water Capital Reserve Fund is a separate fund from the Utility's depreciation fund, which is restricted to be used only for capital works. Ms. Crowell explained that the fund is an accumulation of past operating surpluses which the Commission felt would be prudent to set aside to be used in the case of the occurrence of an unexpected, unbudgeted event.

[37] The revised Rate Study, filed in response to the IRs, indicated the depreciation fund balance would be \$242,966 at the end of the Test Years after deducting funding for the capital projects from depreciation, as outlined above. The response to Undertaking U-1, with the additional depreciation associated with the donated assets, projects this balance to be \$348,316.

[38] The Board inquired about the line item "Due to Depreciation Reserve Fund" in the amount of \$5,000 in each of 2014/15 and 2016/17 and \$4,000 in 2015/16, indicated in the Projected Capital Fund Balance Sheet filed in response to the IRs. Ms. Crowell noted that this relates to capital funding that was taken from the Utility's 2012/13 financial statements and was extrapolated over the Test Years. She added that this amount would normally be zero but in this case there must have been capital funding late in the year which could not be transferred before the end of March.

Findings

[39] The Board accepts the Utility's proposed funding in the Test Years through the capital reserve fund, depreciation and capital from revenue and is pleased that the Utility has included annual expenditures associated with infrastructure renewal. The Board encourages the Utility to seek external funding opportunities as they become available in order to increase its renewal efforts.

[40] The Board finds the Utility's capital reserve, as explained during the hearing, to be a prudent use of funds. It is noted that the capital reserve fund balance at the end of the 2012/13 fiscal year is \$327,679, as indicated in the Utility's financial statements. The Board reminds the Utility that the use of these funds for capital

expenditures requires Board approval, similar to the required approval for the use of depreciation funds.

[41] The Utility is projecting a healthy depreciation fund reserve balance at the end of the Test Period, with the proposed funding. It appears that the amount indicated to be due to the depreciation fund in the projected financial information may have been extrapolated in error. However, the Board reminds the Utility that the depreciation fund should be fully funded each year and presented in the financial statements as set out in the *Accounting Handbook*.

[42] The Utility's response to Undertaking U-1 included a request for formal approval, pursuant to s. 35 of the *Act*, of the addition of the \$2.36 million in donated assets associated with the watermain extension project, which the Board approves. The Board accepts the remainder of the capital items presented in each of the Test Years. The Utility is reminded that inclusion of these proposed capital projects in the Rate Study does not constitute Board approval of these projects. Separate Board approval is required prior to construction for all capital projects in excess of \$250,000 as set out in s. 35 of the *Act*.

3. Non-operating Revenue and Expenditures

[43] The Rate Study included two items of other operating revenues which are projected to remain constant over the Test Period: sprinkler service (\$9,200); and other revenue (\$4,000), which is the interest charged on overdue accounts.

[44] The projected non-operating revenue, in the annual amount of \$5,500 relates mainly to revenue received for work done for Utility customers, identified as jobbing.

[45] The non-operating expenditures include the principal and interest charges associated with the existing debt, which relate to the Utility's three year well field development project, and the reservoir project indicated in the Rate Study in 2013/14. Other annual projected non-operating expenditures are: discount on the debenture issue (\$3,600); private work (\$3,000); interest on customer deposits (\$250); capital out of revenue, as discussed above; and dividend to owner (\$100,000).

[46] The Utility explained the discount on debenture item as being due to it receiving a debenture at a value less than its face value which is amortized over the term of borrowing and brought into the Utility's expenses. The private work is the expense related to the revenue noted above of doing work for Utility customers (jobbing).

[47] Mr. Isenor noted that the requested dividend to owner represents a continuation of the amount which has been paid by the Utility for a number of years.

[48] The revised Rate Study filed in the IR responses, which corrected the annual depreciation expense in the Application, calculated a return on rate base of 4.89%, 5.08% and 4.92%, in each of the Test Years, respectively. Mr. Isenor noted that the return on rate base calculated in the response to Undertaking U-1, which includes the \$2.36 million in donated assets, will not change.

Findings

[49] The Board accepts the other and non-operating revenue as projected in the Rate Study. The Board further accepts the non-operating expenses, including the debt charges, which relate to past debt with no new debt projected over the Test Years,

a continuation of the dividend to owner, and the capital from revenue amounts, used to fund the Utility's capital budgets.

[50] The return on rate base calculated in the Rate Study filed in the response to Undertaking U-1 is the same as those included in the IR response for each of the Test Years, as noted above, which the Board finds to be reasonable.

IV ALLOCATION OF REVENUE REQUIREMENTS

1. Public Fire Protection

[51] The methodology used in the Rate Study to determine the public fire protection charge is consistent with the *Accounting Handbook* as well as the methodology used by the majority of other water utilities in Nova Scotia. The revised Rate Study filed in response to the IRs corrects an error in the allocation of utility plant in service to fire protection, resulting in percentages in the 46.4% to 46.6% range over the Test Years. This can be compared with the range of 47.9% to 48.6% in the last rate application. This reduction in allocation, which the Utility explained is due to the previous application containing the estimated expenditure for the new reservoir which was constructed below budget, results in a proposed decrease in the public fire protection charge. Mr. Isenor noted that the allocation of utility plant in service to fire protection that will be calculated in the response to Undertaking U-1 will be closer to the percentage in the previous application, but it will still result in a reduction of the charge from the current level.

[52] The fire protection charge is to be allocated between the Town and the County based upon the number of hydrants in each jurisdiction. There are currently 252

hydrants in the Town (68.5%) and 116 in the County (31.5%). This is comparable to the allocations in the previous application of 66.4% and 33.6%, respectively.

Findings

[53] The Utility has used the methodology as set out in the *Accounting Handbook* which resulted in a decrease in the public fire protection charge in the first of the three Test Years. This is due to the current charge being based upon a higher than actual cost to construct the new reservoir. The fire protection charges calculated in the response to Undertaking U-1, while higher than those proposed in the Application, continue to propose a decrease in the first Test Year.

[54] The revised fire protection charges filed in response to Undertaking U-1 are based upon the actual reservoir cost, corrected depreciation expense, and the transfer of the \$2.36 million in donated assets. Based upon this, the Board accepts the fire protection charges as set out in the Rate Study filed in response to Undertaking U-1.

2. Utility Customers

[55] The remaining revenue requirements, after the allocation to fire protection charges, are to be recovered from the rates to the Utility's customers. The methodology used to allocate the remainder of the expense amounts to determine the base and consumption charges is consistent with the *Accounting Handbook*, and consistent with the methodology used in the Utility's last rate application.

[56] The Application proposed to transfer amounts of \$21,000 and \$4,000 from the consumption charge to the base charge in each of 2014/15 and 2015/16, respectively, for rate design purposes. The Utility explained the purpose of the transfer

is to prevent the base charge from decreasing by over 9% in the first Test Year, followed by increases of 2.9% and 1.6% in the following years, which Mr. Isenor noted is of concern to customers. He added that while other scenarios were considered to deal with the issue, it was felt that the transfers proposed represent a reasonable balance.

[57] The Utility has experienced growth of approximately 150 customers since the 2009/10 application. Mr. Isenor noted that the rate of growth has declined recently, which is the basis of the projected growth during the Test Years, which he described as reasonable.

[58] The Application noted that the average consumption for a 5/8" meter (residential) customer has been decreasing annually by approximately 3% since the last rate application. Based upon this, the Rate Study projects an annual decrease in residential consumption of 2% in the Test Years. The other metered consumption is projected to remain constant at the current level in each of the Test Years. Mr. Isenor noted that although there has been a drop in water sales overall, without knowledge of the industries associated with the larger meter sizes, it was difficult to draw any conclusions for projection purposes.

[59] The Utility currently has a two block consumption rate structure, with the cut-off between the first and second block at 140,000 gallons per month, which is proposed to remain. The Utility noted that, although there have been discussions to eliminate the block rate, based on feedback received it was decided to maintain the current structure, which can serve as a development incentive. The Utility has eight customers with consumption in the second block.

[60] Mr. Isenor stated that, in his opinion, the rates proposed, which he described as exceptionally low in comparison to others in the province, are just and reasonable. He added that the revised Rate Study filed in response to Undertaking U-1 would result in very little impact on the rates proposed in the Application.

Findings

[61] The allocations of the expenses to the base and consumption charges are in accordance with the *Accounting Handbook* and are consistent with those previously used and are accepted by the Board. The Board accepts the allocations and the transfers from the consumption charge to the base charge, which eliminates fluctuations in the base charges.

[62] It has been a trend in water utilities across Nova Scotia to see decreasing water consumption volumes, even with increased number of customers. The Board accepts the projected consumption volumes, including retaining the block consumption rates, and the number of customers, as set out in the Application, and in the revised Rate Study filed in the response to Undertaking U-1.

V MISCELLANEOUS RATES AND CHARGES

[63] In addition to the rates for water supply to its customers, the Schedule of Rates and Charges includes a number of miscellaneous rates and charges. The Utility noted that the only change proposed is the addition of Item 13 'Charge for Collection Visit' which has a \$25 charge for visits by Commission staff to a customer whose account is in arrears. The Utility explained that the purpose of the charge is to recover the cost of such visits.

Findings

[64] The Board has reviewed the proposed charges and approves the miscellaneous charges as filed.

VI SCHEDULE OF RULES AND REGULATIONS

[65] The Application proposed one change to the Schedule of Rules and Regulations, namely the addition of Regulation 5 'Billing'. Mr. Isenor explained that this Regulation gives clarity to Utility staff with respect to prorating bills. He added that it has been added to the Regulations of a number of utilities which have had recent rate applications.

[66] In response to the IRs, the Utility corrected an error in the definition of meter rate service, which should read as follows to conform with the current definition:

"Metered Rate Service" means that type of service charged for at metered rates. Metered rate service is required for all new services.

[67] The Utility indicated that it currently has an active program in place to determine and mitigate the potential associated risks with respect to Regulation 20 'Cross Connection Control & Backflow Prevention'.

Findings

[68] The Board approves the Utility's Schedule of Rules and Regulations, as proposed, with the correction to the definition of "Metered Rate Service", as set out in the response to the IRs. The Board is pleased that the Utility has developed a cross connection control program.

VII CONCLUSION

[69] The Board approves both the Utility's request to acquire the \$2.36 million of assets funded by the County, and the revised Rate Study filed in response to Undertaking U-1, which includes the transfer of these assets to the Utility in 2014/15.

[70] The increases for an average residential customer in the response to Undertaking U-1 are 5.3%, 2.3% and 1.1%, respectively in each of the Test Years, which are similar to those proposed in the Application. The amendments to the public fire protection charge in the response to Undertaking U-1 are -6.3%, 4.6% and 1.5%, respectively, over each of the Test Years.

[71] Accordingly, the Board approves the Schedule of Rates for Water and Water Services, as set out in the revised Rate Study filed in response to Undertaking U-1, effective May 1, 2014, April 1, 2015 and April 1, 2016. The approved public fire protection charge is prorated at one month at the current rate and 11 months at the new rate.

[72] The Board approves the Schedule of Rules and Regulations, with the revisions noted above, with an effective date of May 1, 2014.

[73] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, this 10th day of April, 2014.



Peter W. Gurnham