

M A N I T O B A) Order No. 136/14
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THE PUBLIC UTILITIES BOARD ACT) December 8, 2014

BEFORE: Susan Proven, P.H.Ec., Acting Chair
The Hon. Anita Neville, P.C., B.A. (Hons.), Member

TOWN OF LYNN LAKE
WATER AND SEWER UTILITY
ACTUAL DEFICITS 2011, 2012, 2013 AND ANTICIPATED DEFICIT 2014

WHEREAS the Public Utilities Board (Board) issued Order No. 151/08 on November 7, 2008 requiring all water and/or sewer utilities to report an actual year-end deficit to the Board if the utility:

1. had not received prior approval for the deficit from the Board and such deficit either exceeds \$10,000 or represents 5% of the utility's operating budget; or
2. had received prior approval for the deficit from the Board and the actual deficit:
 - a. exceeds the previously approved amount by either \$10,000 or 5% of the utility's operating budget; or
 - b. is caused as a result that differs from that upon which said approval was granted;

AND WHEREAS the Town of Lynn Lake Water and Sewer Utility incurred a deficit of \$48,609 at the end of the 2011 operating year, when calculated for regulatory purposes;

AND WHEREAS the Town of Lynn Lake Water and Sewer Utility incurred a deficit of \$149,367 at the end of the 2012 operating year, when calculated for regulatory purposes;

AND WHEREAS the Town of Lynn Lake Water and Sewer Utility incurred a deficit of \$203,004 at the end of the 2013 operating year, when calculated for regulatory purposes;

AND WHEREAS the Town of Lynn Lake Water and Sewer Utility applied for approval of a budgeted deficit of \$112,950 for the 2014 operating year;

AND WHEREAS it is proposed that the reasons for said deficits are increased operating costs, Public Sector Accounting Board impacts, in addition to a budgeted net operating deficit;

AND WHEREAS it is proposed that the 2011 and 2012 deficits not be recovered in whole or in part;

AND WHEREAS it is proposed that the 2013 deficit be recovered by a three (3) year rate rider of \$20,000 per year, calculated per residential equivalency unit (REU) and a five (5) year tax levy calculated by mill rate, totalling \$143,004.

AND WHEREAS it is proposed that the 2014 deficit be recovered by a one (1) year rate rider totalling \$7,000 calculated per residential equivalency unit (REU); a transfer from the Town's general operating fund totalling \$100,000; and a one (1) year tax levy calculated by mill rate, totalling \$5,950.

Application

The applications from the Town of Lynn Lake (Town) for approval of the 2013 and 2014 operating deficits were received June 25 and July 25, 2014, respectively. The applications state that the deficits are a result of numerous operational factors, such as increased distribution costs, high operating costs due to the age of the water distribution network and difficulties with the water treatment plant.

The former CAO advised the Board that the Utility was experiencing serious operational issues with the new water treatment plant. It was implied that the selected water treatment process may not be optimal to treat water to drinking water standards. This has resulted in operating costs many times higher than they should be, putting the Utility in a deficit position.

Upon review of the deficit applications, the Board sent a round of questions to the Town on September 8, 2014. Responses and a copy of the 2013 audited financial statements were received by the Board on October 16, 2014.

The Board has long been a proponent of the user-pay principle, and in the first round of questions asked the Town to provide the rationale for recovering \$148,954 of the Utility deficit through taxes rather than utility rates. The Town responded that they proposed to collect the levy using a mill rate, and the rationale for collecting through taxes rather than utility rates was that there is not room to recover the deficit completely through rates when they anticipate needing a rate

increase. The Town went on to explain that the rationale for not extending the rate rider from three years to five was that it would be unfair as the population of customers changes and would not address the utility's need to recover the deficit in a somewhat timely fashion.

The Board also requested information regarding the 2011 and 2012 deficits. An application for approval of an anticipated deficit for 2012 was submitted by the former CAO in August 2012. After discussing the reasons for the deficit, the application was put on hold because many of the expenses in question were possibly capital in nature. These expenses were largely related to the water treatment plant issues.

In August 2013 the CAO responded that the expenses were not capitalized and forwarded the unaudited financial statements for 2012. At that time, the Board advised that a deficit application accompanied by a Council resolution would be required, and no further communication was received from the Town until June 2014, when the interim CAO filed a deficit application for 2013, and provided a copy of the 2012 audited financial statements. The application also included a Schedule 9, prepared for regulatory purposes, for the years 2009 to 2013. This submission revealed that the Town had experienced significant deficits in all of the years presented.

In March 2011 the Board approved revised rates on an interim *ex parte* basis, which were then varied and confirmed as final in September 2011, in Board Order Nos. 46/11 and 123/11, respectively. The rate study included in the 2011 rate

application recommended a rate rider of \$85.00 per year to help address the Town's accumulated utility deficits. The Town did not propose to implement this rate rider, with the rationale that the Town was in the process of seeking funding from the Provincial Government through the Mining Community Reserve Fund (MCRF).

The Board agreed with the Town that the MCRF funding should be accessed to help address the issue, but expressed concern over the lack of response from the MCRF. The Board did not impose the rate rider, with the "...proviso that the Town actively pursues an official response from the MCRF. Should no response be received by March 31, 2012, the Board will reconsider the rate rider." There is no indication in the file that the Town followed up with the Board, and the interim CAO advises the Board that no additional funding from the Provincial Government is anticipated at this time.

The Town has passed a Council Resolution regarding the 2011 and 2012 deficits stating that, "Council directs the CAO to file Deficit Recovery Applications with the PUB for the years 2011 and 2012 that do not recover the incurred deficits in whole or in part."

Working capital calculation

Board Order No. 93/09 established that utilities should maintain a minimum working capital surplus, in an amount equal to 20% of annual expenses. The working capital surplus is defined as the Utility fund balance, excluding any capital related items plus Utility reserves.

	2013
Fund surplus	\$ 1,225,011.00
Deduct tangible capital assets	\$ 2,941,794.00
Add long term debt	\$ 137,523.00
Add utility reserves	\$ 209,864.00
Working capital surplus (deficit)	\$ (1,369,396.00)

Board findings

By law, Manitoba utilities are not allowed to incur deficits. In the event that a deficit does occur, the Utility is required to obtain Board approval for a recovery methodology. The utility is in a serious working capital deficit position, caused by years of unresolved deficits.

The problems associated with declining population, including fewer customers to pay for utility operations, are not new to the Board. Depopulation is a significant problem faced by some other utilities in Manitoba. Notwithstanding these circumstances and the pressure placed on ratepayers, there remains a duty of care for the Town to operate the utility in a safe manner, so as to further the health, welfare and economic development of the Town. The Board is sensitive to customer reaction to the magnitude of the rate riders, however, must

consider the sustainability of the Utility when approving deficits and rate applications.

While the Town and Board were hopeful that the MCRF funding would provide some much needed financial relief to the Town's ratepayers, deferring the recovery has now put the Utility in a worse financial position. This has been compounded by continued depopulation, operational challenges with the new water treatment plant and human resource constraints at both the Town and the Board.

The Board recommends that the Town work with the Manitoba Water Services Board and any other resources they may have to resolve the challenges being experienced with the water treatment plant. The Board is deeply concerned by Council's Resolution requesting that deficits be left unrecovered. Despite the financial pressures this recovery will place on the ratepayers, action must be taken to resolve the matters facing this Community and Utility. Doing nothing is not an option.

The Board will vary the Town of Lynn Lake's application for approval of the 2011, 2012, 2013 and 2014 operating deficits.

The Board agrees with the Town's argument that the recovery should not extend past five years, but disagrees with the rationale behind collecting the deficit through taxes. The Board believes that a rate rider sends a clearer pricing signal to users of the Utility, and also ensures that deficits are recovered on a fairer basis than the use of taxes levied by mill rate.

To address the Town's concern that the Utility would not recover the deficits in a somewhat timely fashion, the Board has adjusted the recovery periods to allow for the same amount of revenue as proposed by the Town, rather than simply splitting the recovery equally over a five (5) year period. The recovery of the 2012 deficit is over and above the original proposal, and is split equally over the five (5) year period.

The Board will direct the Town to recover the 2012, 2013 and 2014 deficits using following schedule, calculated using 387 REUs:

2012, 2013 and 2014					
	Year 1	Year 2	Year 3	Year 4	Year 5
Rate rider	\$ 91,423	\$ 78,473	\$ 78,473	\$ 58,473	\$ 58,473
Transfer	\$100,000				
Total	\$191,423	\$ 78,473	\$ 78,473	\$ 58,473	\$ 58,473
Rate rider					
Per REU	\$ 236.24	\$ 202.77	\$ 202.77	\$ 151.09	\$ 151.09
Quarterly	\$ 59.06	\$ 50.69	\$ 50.69	\$ 37.77	\$ 37.77

The Board notes that the recovery of the 2011 deficit through a transfer from reserve funds of \$89,492 has already taken place and will not require further action from the Town.

As stated above, the Board is a strong proponent of the user pay system, and in general does not approve of cross subsidization. The Board feels that the Town does appear to have reached a crisis situation, and will approve a onetime transfer of \$100,000 from the general operating fund to offset a portion of the 2014 deficit. The Town should not take this as a signal

that the Board finds this to be an acceptable practice, nor as approval to continue this transfer in years to come.

The Town advises that the number of Residential Equivalency Units (REUs) assigned is 387, one REU being the volume of water estimated to be used by the average single family residence. Units allocated to other customers are based on estimated water they will use, as compared with a residence. REUs are used in communities with unmetered distribution and collection systems, where information regarding actual consumption is unavailable. Should the number of REUs assigned change during the five year period the rate rider would also change, based on a revised calculation.

It is the Board's understanding that the Town's interim CAO will be leaving his position effective December 19, 2014 and at this time no replacement has been engaged. This is cause for concern, particularly given failure to comply with information requests in the past. The Board must therefore emphasize to the Town that it is imperative that the directives included in this Order be followed.

Pursuant to the *Public Utilities Board Act*, the Board has available enforcement methods and can apply penalties. The Board will consider utilizing the means at its disposal if the Town fails to comply with this Order.

IT IS THEREFORE ORDERED THAT:

1. The 2012, 2013 and 2014 deficit recovery for the Town of Lynn Lake Water and Sewer Utility Operations, is HEREBY APPROVED to be recovered by a rate rider of \$91,423 (\$59.06 per REU at 387 REUs) to be collected on a quarterly basis for four (4) quarters beginning April 1, 2015;
2. The 2012, 2013 and 2014 deficit recovery for the Town of Lynn Lake Water and Sewer Utility Operations, is HEREBY APPROVED to be recovered by a rate rider of \$156,946 (\$50.69 per REU at 387 REUs) to be collected on a quarterly basis for eight (8) quarters beginning April 1, 2016;
3. The 2012, 2013 and 2014 deficit recovery for the Town of Lynn Lake Water and Sewer Utility Operations, is HEREBY APPROVED to be recovered by a rate rider of \$116,946 (\$37.77 per REU at 387 REUs) to be collected on a quarterly basis for eight (8) quarters beginning April 1, 2018;
4. The 2014 deficit recovery for the Town of Lynn Lake Water and Sewer Utility Operations, is HEREBY APPROVED to be recovered by a transfer of \$100,000 from the Town's general operating fund;
5. The Town of Lynn Lake is to provide notice to its customers, with a copy to the Board, of the deficit recovery before the beginning of the next quarterly billing period;

6. The Town of Lynn Lake is to file a revised rate application on or before June 30, 2015.

Fees payable upon this Order - \$150.00

THE PUBLIC UTILITIES BOARD

"SUSAN PROVEN, P.H.Ec."
Acting Chair

"JENNIFER DUBOIS, CMA."
Acting Secretary

Certified a true copy of
Order No. 136/14 issued by
The Public Utilities Board

Acting Secretary

Board decisions may be appealed in accordance with the provisions of Section 58 of *The Public Utilities Board Act*, or reviewed in accordance with Section 36 of the Board's Rules of Practice and Procedure (Rules). The Board's Rules may be viewed on the Board's website at www.pub.gov.mb.ca.