

M A N I T O B A) **Order No. 119/14**
)
THE PUBLIC UTILITIES BOARD ACT) **October 29, 2014**

BEFORE: Régis Gosselin, B ès Arts, MBA, CGA, Chair
Marilyn Kapitany, B.Sc. (Hon), M.Sc., Member
Neil Duboff, BA (Hons), LLB, TEP, Member

STITTCO UTILITIES MAN LTD.
NON-COMMODITY COSTS
EFFECTIVE NOVEMBER 1, 2014
FINAL APPROVAL

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1.0 EXECUTIVE SUMMARY

By this Order, The Public Utilities Board (Board) approves the non-commodity rates for Stittco Utilities Manitoba Ltd. (Stittco) effective November 1, 2014. The Board also approves the rate base for Stittco as of July 31, 2014 and confirms as final the commodity rates previously approved on an interim ex parte basis. Non-commodity rates will be increased by 5.4% effective November 1, 2014.

Non-commodity costs include costs incurred by Stittco for the distribution of propane to customers. In accordance with Board Order 141/08, non-commodity costs are reviewed annually, with allowed costs recovered in rates through a basic monthly charge and a delivery charge which is based on consumption.

The Board accepts Stittco's projected annual non-commodity cost of \$1,897,421 for the year ending July 31, 2015. This is an increase of \$150,040 over \$1,747,381, which was the last non-commodity cost approved by the Board in Order 125/13. The increase in Non-Commodity Costs is largely due to projected increases in costs for wages and benefits, and operating costs. Wages and benefits cost increases are primarily due to the implementation of a new employee pension plan in 2014 and incremental salary increases. Operating costs increases are due to a projected increase in costs for annual leak surveys of the distribution system and vaporizer consumption necessary to convert liquid propane to a gas for distribution to the customer.

The Board also approves Stittco's rate base of \$1,828,831 up from the \$1,708,951 approved in Order 125/13. Rate base is the value of property upon which the utility is allowed to earn a specified rate of return. The Board approves a rate of return of 10% on Stittco's rate base.

Stittco's customer base and propane volumes have steadily declined over the last number of years. In 2009 Stittco had 950 customers and propane sales of approximately 8,631,000 litres. For the 2015 fiscal year, Stittco is projecting a total of 843 customers and propane sales of 6,625,000 litres. This decline in customer numbers and propane volumes results in fewer customers available to share the increase in non-commodity costs.

The Board will expect Stittco to make every effort to manage its operating costs to minimize future non-commodity cost rate increases to their customers. Currently, non-commodity costs account for almost 50 percent of the total billed rate to consumers depending on the price of propane.

Propane commodity costs are set quarterly, pursuant to the Board approved Quarterly Rate Setting (QRS) process. Commodity costs, including transportation to Thompson, are passed on to customers with no mark-up. Variances are tracked in a Propane Purchase Variance Account (PPVA), and are either refunded to (when rates charged are higher than the cost of propane) or collected from (when rates charged are lower than cost) customers in subsequent quarterly rate setting applications.

The table below compares the propane commodity and non-commodity rates over the last year and provides the revised non-commodity rates effective November 1, 2014:

Table 1 Non-commodity rates - 12 month history					
	Nov 1/13	Feb 1/14	May 1/14	Aug 1/14	Nov 1/14
Basic Monthly Charge	\$10.00	\$10.00	\$10.00	\$10.00	\$10.00
Volumetric Charges per m³:					
Commodity Cost Recovery	\$1.4721	\$2.4958	\$1.5439	\$1.3692	\$1.3575 *
Non-Commodity Cost Recovery - Delivery Charge (monthly volumes)					
first 100 m ³	\$1.27814	\$1.27814	\$1.27814	\$1.27814	\$1.34697
next 400 m ³	\$1.13992	\$1.13992	\$1.13992	\$1.13992	\$1.20132
next 1000 m ³	\$1.07863	\$1.07863	\$1.07863	\$1.07863	\$1.13671
next 2500 m ³	\$0.87389	\$0.87389	\$0.87389	\$0.87389	\$0.92093
over 4000 m ³	\$0.67040	\$0.67040	\$0.67040	\$0.67040	\$0.70650

* As approved in Board Order 118/14

This Order also finalizes interim ex parte commodity rates established in Board Orders 124/13, 7/14, 45/14 and 86/14.

2.0 INTRODUCTION

On July 18, 2014, Stittco applied to the Board seeking approval for an approximate 6% increase in non-commodity costs, effective August 1, 2014. Due to the lateness of the Application, and the need for additional information, the Board did not approve revisions to non-commodity rates for August 1, 2014.

Non-commodity costs consist of costs incurred by Stittco for the distribution of propane to its customers. These costs include operating expenses (salaries, materials and supplies, administrative costs, etc.), depreciation, a provision for corporate income tax and a return on Stittco's rate base for its owners.

The Board last approved non-commodity rates by Order 125/13 issued on October 28, 2013.

Stittco's non-commodity rate application for the year ending July 2015 was managed using a paper-based review process to minimize regulatory costs to the utility and to Stittco customers. Customers were advised of Stittco's Application in September of 2014 by means of a bill insert for August billings. The Board received one customer inquiry from a customer seeking clarification on the Application. No written communications were received by the Board from Stittco customers.

Commodity rates for propane are adjusted quarterly using the Quarterly Rate Setting (QRS) process approved by the Board in Order 141/08 and 45/09. The QRS adjusts Stittco's commodity price for propane August 1, November 1, February 1, and May 1 of each year.

Variances between actual propane costs and estimated propane costs embedded in rates are tracked in a Purchase Price Variance Account (PPVA) and either refunded to customers (when rates charged are higher than the cost propane) or collected from customers (when rates charged are lower than the cost of propane), this all in subsequent rate settings. Regular adjustments to commodity prices help to minimize balances in this account.

Rates established by the QRS are approved on an ex parte basis. That means that they are established by the Board without further public consultation, subject to satisfactory information being filed by Stittco. This approach is considered to be the most reasonable and economical, as the changes are driven by commodity price changes and the process minimizes regulatory costs while providing regular updated price signals to consumers. These Interim Commodity rates for propane are reviewed and finalized annually when Stittco files its Non-Commodity application.

On October 21, 2014 Stittco applied to The Board for a decrease of the propane commodity rates from \$1.3692/m³ to \$1.3575/m³. Board Order 118/14 approved the propane commodity rate decrease.

3.0 APPLICATION

Non-Commodity Rates

On July 18, 2014 Stittco applied to the Board for an Order fixing non-commodity rates for all gas customers served by Stittco, requesting an effective date of August 1, 2014.

The application included:

- a) A determination of the non-commodity cost revenue requirement of the company;
- b) A determination of the rate base of Stittco as of July 31, 2014.

In its application, Stittco noted the most recent Board Order relating to non-commodity costs was Board Order 125/13 dated October 28, 2013. This Order determined the non-commodity revenue requirement of the company and finalized non-commodity rates effective November 1, 2013.

In Board Order 141/08, the Board stated:

Going forward, subsequent to the Board finalizing the rate schedule now set on an interim basis, the Board anticipates that future rate reviews will also be handled by the Board's paper-based process. For the annual non-commodity review, the Board will expect Stittco to issue a notice to its customers concurrent with providing the Board with its application, that notice to be pre-vetted by the Board and to provide for customers with concerns writing the Board. Quarterly commodity rates changes will be reviewed by the Board and communicated to customers by Stittco in accordance with future directions of the Board.

In accordance with Board Order 141/08, the Board decided to review the non-commodity cost application using a paper-based process.

Stittco notified its customers of the proposed non-commodity cost rate increase in an information insert included with the September 2014 billing for August propane consumption. Customers were advised that they could contact either Stittco or the Board to review the Application and to express their concerns. The Board received one customer telephone call seeking clarification on Stittco's Application. The Board received no written communication related to the Application.

On September 12, 2014, the Board submitted Information Requests to Stittco; Stittco responded on September 26, 2014.

Stittco's 2014 submission for non-commodity costs projected a 2014 non-commodity cost revenue requirement of \$1,897,421. This represents an increase of \$150,040.00 over that approved by the Board in Order 125/13 for the year ending July 31, 2014.

The table below summarizes Stittco's projected non-commodity revenue requirement for the year ending July 31, 2015 and compares it to non-commodity costs approved in Board Order 125/13 for the year ending July 31, 2014.

	Stittco Application Jul-14	Approved From Board Order 125/13	Increase Decrease
Wages & Benefits	764,220.00	666,760.00	97,460.00
Materials and Supplies	49,500.00	47,600.00	1,900.00
Contract Services	100,950.00	101,600.00	-650.00
Other Operating Costs	131,500.00	103,500.00	28,000.00
Automotive	53,160.00	44,750.00	8,410.00
Insurance	60,000.00	75,000.00	-15,000.00
Property Taxes	118,000.00	118,000.00	0.00
Administrative & General	232,876.00	204,740.00	28,136.00
Total Direct	1,510,206.00	1,361,950.00	148,256.00
Administration Fee	173,125.00	163,434.00	9,691.00
Total Direct Operating Costs	1,683,331.00	1,525,384.00	157,947.00
Other Cost of Sales	120,000.00	120,000.00	0.00
Depreciation	97,177.00	115,185.00	-18,008.00
Accretion	27,560.00	27,560.00	0.00
Return on Rate Base	182,883.00	170,895.00	11,988.00
Income Tax Requirement	61,070.00	62,957.00	-1,887.00
Other Income	-274,600.00	-274,600.00	0.00
Total Other Costs	214,090.00	221,997.00	-7,907.00
Non-Commodity Revenue Requirement	1,897,421.00	1,747,381.00	150,040.00

Overall, Stittco's total *direct* operating costs for 2015 are expected to increase by \$157,947 over those approved in Board Order 125/13. Stittco's *other* costs are expected to decrease by \$7,907 over those approved in Board Order 125/13. The *total* non-commodity revenue requirement is expected to increase by \$150,040 over the currently approved costs.

Non-Commodity Cost Requirement

The largest single increase in projected non-commodity costs is for wages and benefits. Stittco's Application is projecting an increase of wage and benefit costs from \$666,760.00 (approved in Board Order 125/13) to \$764,220. This represents an increase of \$97,460.00. A large part of this increase is due to the introduction of a new company pension program implemented by Stittco in July 2014. Stittco's portion of the new pension plan is expected to cost \$48,000.00. Stittco states this employee pension plan was introduced to allow Stittco to stay competitive in the local marketplace and provide a base pension retirement program to employees. The remainder of the increase attributable to wages and benefits arises from projected increases in employee compensation and benefit costs.

Other major non-commodity cost increases include a projected increase in operating costs of \$28,000 from \$103,500.00 (approved in Order 125/13) to \$131,500.00 in the current Application. This increase in operating costs is primarily due to a projected increase in costs for leak surveys of the distribution system (a \$12,000.00 increase) and vaporizer consumption costs (a \$16,000.00 increase). Leak surveys are conducted annually by an independent contractor who has advised Stittco of cost increases for 2015. Vaporizer costs increases are due to the projected higher costs of propane consumed by vaporizer equipment.

Stittco also projects an increase in automotive costs by approximately \$8,400 for 2015 largely due to an increase in maintenance and fuel costs.

Stittco's administrative costs are projected to increase by \$28,136 from \$204,740 (approved in Order 125/13) to \$232,876. Most of this cost increase is due to a projected increase in consulting fees to upgrade Stittco's billing system (\$15,000) and legal fees (\$5,000). Stittco has also projected an increase of \$3,500 for staff training.

Stittco projected cost reductions of \$15,000 in insurance requirements and \$18,000 in depreciation costs versus costs approved in Board Order 125/13.

Stittco's projected midyear rate base for 2015 is \$1,828,831. The current approved rate base from Board Order 125/13 is \$1,708,951. Stittco's rate base has increased largely due to investments made by Stittco in their propane storage facility.

In its Application, Stittco seeks to continue the 10% return on the projected rate base. This would result in an annual revenue requirement of \$182,883. Stittco holds the view that given the investment risk, an appropriate rate of return would be significantly higher than the approved 10%. However, Stittco acknowledges that it operates in a very competitive market in a small service area. Stittco's primary competition is from customer's who may choose electricity as their option for space heating rather than propane. At current rates, electricity is a much more cost effective option than propane.

In recent years, Stittco's actual returns have generally been less than the 10% return provided for in rates. Stittco's return on rate base for the past ten years is provided in the chart below:

Table 3 Rate of return- 10 year history				
Year	Mid – Year Rate Base	Actual Return (Loss)	Actual % Return	Normalized % Return*
2013	\$1,733,824	\$258,248	14.9%	13.78%
2012	\$1,953,864	\$67,310	3.44%	10.02%
2011	2,051,484	111,698	5.44%	6.72%
2010	1,980,700	(160,751)	(8.12)%	(0.48)%
2009	2,009,574	112,030	5.57%	4.10%
2008	2,138,167	(11,520)	(0.54)%	(1.99)%
2007	1,927,450	(88,036)	(4.57)%	(0.81)%
2006	1,937,865	(93,102)	(4.80)%	0.03%
2005	1,929,813	83,480	4.33%	4.76%
2004	1,897,533	169,904	8.95%	10.29%
2003	2,039,653	223,741	10.97%	11.92%

* adjusted to eliminate variances due to weather fluctuations

Stittco's projected return for the year ending July 31, 2014 is 10.58%. Stittco acknowledges in their Application that the 2013 actual return (14.9%) and 2014 projected return (10.58%) is largely contingent on two factors. The first is a one-time construction load (122,000 litres in 2014 and 428,560 litres in 2013) and a colder than normal winter. Adjusting for these construction loads and normalizing returns for weather, Stittco would have returned 13.78% in 2013 and a projected 9.63% in 2014.

4.0 STITTCO OPERATIONS

Stittco Utilities Manitoba Inc. distributes propane through a pipeline distribution network to approximately 830 customers in Thompson, Flin Flon and Snow Lake, Manitoba. Bulk propane is supplied from Edmonton and is shipped to Stittco's storage facilities by rail or by truck.

Stittco's historical and projected propane sales base is described in the table below:

Table 4 Propane sales- historical and projected					
		Residential	Commercial	Total	Change
2009	Customers	784	166	950	
	Propane Volumes	2,161,828	6,468,853	8,630,681	
2010	Customers	770	164	934	-1.7%
	Propane Volumes (l)	1,735,190	5,365,294	7,100,484	-17.7%
2011	Customers	749	163	912	-2.4%
	Propane Volumes (l)	1,864,586	5,230,726	7,095,312	-0.1%
2012	Customers	740	162	902	-1.1%
	Propane Volumes (l)	1,663,000	5,207,000	6,870,000	-3.2%
2013	Customers	732	163	895	-0.8%
	Propane Volumes (l)	1,865,000	5,324,100*	7,189,100*	4.6%
2014	Customers	690	153	843	-5.8%
	Propane Volumes (l)	1,810,000	5,280,000*	7,090,000*	-1.4%
2015 projected	Customers	690	153	843	0.0%
	Propane Volumes (l)	1,740,000	4,885,000	6,625,000	-6.5%

* Includes non-recurring construction load

As can be seen from this table, both the number of customers and propane volumes are steadily declining. Propane volumes increased slightly in 2013 and 2014 largely due to a one-time construction load.

Historically, residential customers have accounted for approximately 25% of the overall propane volumes sold by Stittco, with commercial customers accounting for the remaining 75%.

The Stittco residential customer base has been gradually declining over the last few years, as has its commercial customer base. The commercial customer numbers declined significantly in 2014 as a result of the conversion of several apartment buildings to electrical heat and the closing of a large commercial business. The residential decline has generally been attributed to the difference in cost between heating with propane versus heating with electricity. Heating with propane can be two to three times the cost of heating with electricity depending on propane costs and furnace efficiency.

5.0 BOARD FINDINGS

Non-commodity rates

The Board has reviewed Stittco's application for non-commodity costs of July 2014, as well as Stittco's responses to interrogatories posed by the Board.

The Board hereby approves the non-commodity rate application filed by Stittco for non-commodity rates effective November 1, 2014. The Board finds Stittco's revenue requirements to be reasonable. Stittco's implementation of a new Company pension plan, at a projected cost of \$48,000, represents one of Stittco's largest projected increases in operating costs for 2015, and therefore revenue requirement. Other significant operating cost increases, such as annual leak surveys (increase of \$12,000), vaporizer consumption (increase of \$16,000) and consulting fees (increase of \$15,000) are significant but necessary for the operation of the distribution system and billing collection system. The Board, however, is concerned about the continued rise in operating and administration costs. This is further compounded by a decline in customer numbers and propane volumes. The impact of these two factors is future cost increases must be paid by smaller number of customers resulting in larger increases in non-commodity rates. The Board expects Stittco to make every effort to control its operating costs to minimize future rate increases to customers.

The Board agrees that Stittco should receive a reasonable return on its investment. The Board will therefore approve Stittco's rate base of \$1,828,831 and a 10% return on rate base amounting to \$182,883. This rate base has increased approximately \$120,000 in value in 2014 largely due to investments by Stittco in bulk storage tanks and related work equipment.

Commodity rates

The quarterly rate setting process for commodity costs appears to continue to serve customers well, with the periodic rate adjustment helping to mitigate rate shock due to fluctuating commodity market prices. The Board continues to recommend that customers seek ways to upgrade the heating efficiency of their premises, so as to reduce consumption, bills and carbon emissions. The Board notes that the current cost of heating an average residential dwelling with propane is 2 to 3 times the average cost of heating by electricity depending on heating efficiencies.

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 reviewed on the Board's website at www.pub.gov.mb.ca.

6.0 IT IS THEREFORE ORDERED THAT:

1. Stittco Utilities Manitoba Ltd's rates for distribution costs, as per Schedule "A" for consumption on or after November 1, 2014, **BE AND ARE HEREBY APPROVED.**
2. Stittco Utilities Manitoba Ltd's rate base of \$1,828,831 for 2015 **BE AND IS HEREBY APPROVED.**
3. All interim ex parte orders referenced in Board Orders 124/13, 7/14, 45/14, 86/14 **BE AND ARE HEREBY APPROVED AS FINAL.**

THE PUBLIC UTILITIES BOARD

"Régis Gosselin, B ès Arts, MBA, CGA, "
Chair

"Kurt Simonsen, P.Eng."
Acting Secretary

Certified a true copy of Order No. 119/14
issued by The Public Utilities Board

SCHEDULE" A"

GENERAL SERVICE RATE STRUCTURE
EFFECTIVE FOR CONSUMPTION ON OR AFTER NOVEMBER 1, 2014

Basic Monthly Charge	\$10.00
Volumetric Charges per m³:	
Commodity Cost Recovery	\$1.3575*
Non-Commodity Cost Recovery-Delivery Charge (monthly volumes):	
first 100 m ³	\$1.34697
next 400 m ³	\$1.20132
next 1000 m ³	\$1.13671
next 2500 m ³	\$0.92093
over 4000 m ³	\$0.70650

* Commodity Cost approved per Board Order 118/14