

M A N I T O B A) **Order No. 106/15**
)
THE PUBLIC UTILITIES BOARD ACT) **October 29, 2015**

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

STITCO UTILITIES MAN LTD.
NON-COMMODITY COSTS
EFFECTIVE NOVEMBER 1, 2015
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, 2015. The Board also approves the rate base for Stittco as of July 31, 2015 and confirms as final the commodity rates previously approved on an interim ex parte basis. Non-commodity rates will be increased by approximately 4.4% effective November 1, 2015.

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 and recovered in rates through a basic monthly charge and a delivery charge. Delivery charges assigned based on a customer's monthly consumption of propane.

The Board accepts Stittco's projected annual non-commodity cost of \$2,011,179 for the year ending July 31, 2016. This is an increase of \$113,758 over the last non-commodity cost approved by the Board in Order 119/14 which was \$1,897,421.

The Board also approves Stittco's rate base of \$1,971,455 which is an increase from \$1,828,831 approved in Order 119/14. 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.

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, 2015:

Table 1 Non-commodity rates - 12 month history					
	Nov 1/14	Feb 1/15	May 1/15	Aug 1/15	Nov 1/15
Basic Monthly Charge	\$10.00	\$10.00	\$10.00	\$10.00	\$10.00
Volumetric Charges per m³:					
Commodity Cost Recovery	\$1.3575	\$0.8245	\$0.9558	\$0.4219	\$0.4646
Non-Commodity Cost Recovery - Delivery Charge (monthly volumes)					
first 100 m ³	\$1.34697	\$1.34697	\$1.34697	\$1.34697	\$1.40555
next 400 m ³	\$1.25358	\$1.25358	\$1.25358	\$1.25358	\$1.25358
next 1000 m ³	\$1.18618	\$1.18618	\$1.18618	\$1.18618	\$1.18618
next 2500 m ³	\$0.96097	\$0.96097	\$0.96097	\$0.96097	\$0.96097
over 4000 m ³	\$0.73723	\$0.73723	\$0.73723	\$0.73723	\$0.73723

- Notes to Table: 1/ Non-Commodity costs for November 2014 and February, May and August of 2015 were approved in Board Order 119/14
 2/ The Commodity cost for November 1, 2015 was approved in Board Order 107/15

This Order also finalizes interim ex parte commodity rates established in Board Orders 118/14, 9/15, 42/15 and 78/15.

2.0 INTRODUCTION

On July 20, 2015 Stittco applied to the Board seeking approval for an approximate 5.5% increase in non-commodity costs, effective August 1, 2015. 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, 2015.

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 119/14 issued on October 29, 2014.

Stittco's non-commodity rate application for the year ending July 2016 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 August of 2015 by including the Board's Public Notice of proposed non-commodity rate revisions in Stittco's August billings. The Board did not receive any oral or written customer responses from the Public Notice.

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 of 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 15, 2015 Stittco applied to the Board for an increase of the propane commodity rates from \$0.4219/m³ to \$0.4646/m³. Board Order 107/15 approved the propane commodity rate increase.

3.0 APPLICATION

Non-Commodity Rates

On July 23, 2015 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, 2015.

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, 2015.

In its application, Stittco noted the most recent Board Order relating to non-commodity costs was Board Order 119/14 dated October 29, 2014. This Order determined the non-commodity revenue requirement of the company and finalized non-commodity rates effective November 1, 2014.

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 customers were notified of the proposed non-commodity cost rate increase by including the Board's Public Notice in Stittco's August 2015 billings to customers for September propane consumption. Customers were advised that they could contact either Stittco or the Board to review Stittco's Application and to express their concerns. The Board did not receive any oral or written communication from the public regarding Stittco's Application.

On August 25, 2015, the Board submitted Information Requests to Stittco; Stittco responded on September 14, 2015.

On October 6, 2015 the Board submitted a second round of Information Requests that sought further clarification of selected Round 1 Information Requests. Stittco responded on October 14, 2015.

Based on the results of the Board's Information Requests, Stittco filed an amended Application for non-commodity costs on October 14, 2015. The amended Application included a small reduction in operating costs from \$1,769,426 to \$1,748,782 and a reduction in rate base from \$1,974,043 to \$1,971,455. The reduction in rate base also reduced the projected return on rate base from \$197,404 to \$197,145. The primary reason for reduced operating costs was a reduction in insurance costs and a small reduction in working capital which is included in the calculation of the return on rate base.

The overall impact of these amendments was a reduction in the overall non-commodity rate increase from 5.5% to approximately 4.4%.

The table below summarizes Stittco's projected non-commodity revenue requirement for the year ending July 31, 2016 and compares it to non-commodity costs approved in Board Order 119/14 for the year ending July 31, 2015.

	Stittco's Revised Application Oct-15	Approved From Board Order 119/14	Increase Decrease
Wages & Benefits	800,067.00	764,220.00	35,847.00
Materials and Supplies	57,800.00	49,500.00	8,300.00
Contract Services	107,600.00	100,950.00	6,650.00
Other Operating Costs	113,818.00	131,500.00	-17,682.00
Automotive	69,960.00	53,160.00	16,800.00
Insurance	41,568.00	60,000.00	-18,432.00
Property Taxes	120,000.00	118,000.00	2,000.00
Administrative & General	250,600.00	232,876.00	17,724.00
Total Direct	1,561,413.00	1,510,206.00	51,207.00
Administration Fee	187,370.00	173,125.00	14,245.00
Sub-Total Direct Operating Costs	1,748,783.00	1,683,331.00	65,452.00
Other Cost of Sales	120,000.00	120,000.00	0.00
Depreciation	103,364.00	97,177.00	6,187.00
Accretion	27,560.00	27,560.00	0.00
Return on Rate Base	197,145.00	182,883.00	14,262.00
Income Tax Requirement	88,927.00	61,070.00	27,857.00
Other Income	-274,600.00	-274,600.00	0.00
Sub-Total Other Costs	262,396.00	214,090.00	48,306.00
Non-Commodity Revenue Requirement	2,011,179.00	1,897,421.00	113,758.00

Overall, Stittco's total direct operating costs for 2016 are expected to increase by \$65,452 over those approved in Board Order 119/14. Stittco's other costs are expected to increase by \$48,306 over those approved in Board Order 119/14. The total non-

commodity revenue requirement is expected to increase by \$113,758 over the currently approved costs.

Operating Costs

The largest increase in projected non-commodity costs is for wages and benefits. Wage and benefit costs have risen from \$764,220, as approved in Board Order 119/14, to \$800,607. Actual wage and benefit costs projected to July 31, 2015 are \$774,209. Projected wage and benefit costs therefore amount to an approximate 3.3% increase. Stittco reported these increases are needed to remain competitive with industrial salaries in the region. Stittco also highlights that licensed gas fitters continue to be in demand and salary increases are necessary to retain qualified personnel.

Administration costs have also risen by \$17,724 from \$232,876 approved in Board Order 119/14 to \$250,600. These cost increases are largely attributed to increases in bad debt charges of \$9,000, payroll tax increases of approximately \$3,700 and an increase in bank charges of \$2,500.

Vehicle costs have increased by approximately \$16,800. This represents the cost to lease three service vehicles versus purchasing vehicles. With the purchase of Stittco by Gibson, Stittco will now be part of the Gibson service truck lease program and eligible for preferred lease rates. Leasing vehicles are expected to reduce the otherwise large capital expenses of vehicle purchases.

Stittco has also seen a reduction in costs in the "other operating costs" category. Most of the approximately \$17,700 in savings are attributed to vaporizer consumption efficiency improvements. Stittco has also seen a reduction in insurance costs from a previously approved cost of \$60,000 to \$41,568. This reduction in premium reflects improved rates that can be obtained as a result of becoming part of the larger Gibson/Canwest organization.

Rate Base and Rate of Return

Rate base is the value of property upon which the utility is allowed to earn a specified rate of return. The Board approved a 10% rate of return for Stittco's fiscal year ending July 31, 2015. The Stittco projected mid-year rate base for 2015 approved in Board Order 119/14 was \$1,828,831. Stittco's projected rate base for 2015 in Stittco's current non-commodity cost Application is \$1,792,693. This rate base is lower than that approved by the Board in Order 119/14.

The reduction in rate base for 2015 was due to Stittco's management decision to hold capital spending in 2015 while Stittco conducted a thorough assessment of maintenance programs and the need for replacement of infrastructure. The costs to conduct this assessment was \$120,000 which is reflected in the revised rate base which offset somewhat the capital expenditures planned but not made in 2015. Stittco had originally projected \$150,000 in capital expenditures for the year ending July 31, 2015.

The projected rate base for 2016 is \$1,971,445. The majority of the additions to the rate base arise from replacement of Stittco's unloading towers (\$550,000) plus smaller amounts for computer equipment (\$25,400) and tools and equipment (\$10,000). Total plant additions to the rate base are projected at \$585,400 for 2016. The projected mid-year rate base for 2016 after considering accumulated depreciation and working capital, is \$1,971,455.

Stittco continues to seek a 10% return on the projected rate base. This would result in an annual revenue requirement of \$197,145. 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.

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:

Rate of return- 10 year history				
Year	Mid – Year Rate Base	Actual Return (Loss)	Actual % Return	Normalized % Return*
2014	\$1,708,951	\$235,826	13.50%	7.93%
2013	\$1,733,824	\$258,248	14.90%	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%

* adjusted to eliminate variances due to weather fluctuations

Stittco's projected return for the year ending July 31, 2015 is 12.50%. This return is larger than the target 10% in part due to the smaller mid-year rate base due to curtailment of capital expenditures in 2015.

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:

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	1,735,190	5,365,294	7,100,484	-17.7%
2011	Customers	749	163	912	-2.4%
	Propane Volumes	1,864,586	5,230,726	7,095,312	-0.1%
2012	Customers	740	162	902	-1.1%
	Propane Volumes	1,663,000	5,207,000	6,870,000	-3.2%
2013	Customers	732	163	895	-0.8%
	Propane Volumes	1,865,000	5,324,100*	7,189,100*	4.6%
2014	Customers	690	153	843	-5.8%
	Propane Volumes	1,810,000	5,280,000*	7,090,000*	-1.4%
2015	Customers	690	153	843	0.0%
	Propane Volumes	1,589,000	4,943,000	6,625,000	-6.6%
2016	Customers	690	153	843	0.0
Projected	Propane Volumes	1,707,000	5,016,000	6,723,000	1.5%

As can be seen from the table, the number of customers and propane volumes have generally been 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.

5.0 BOARD FINDINGS

Non-commodity Costs

The Board has reviewed Stittco's Application for non-commodity costs for the fiscal year ending July 31, 2016, 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, 2015. The Board finds Stittco's non-commodity revenue requirement to be reasonable. The Board, however, is concerned about the continued rise in operating and administration costs. This is further compounded by a downward trend in customer numbers and propane volumes. If the trend is maintained, future increased costs will be assessed on diminishing volumes and paid by fewer customers resulting in larger increases in non-commodity rates. Stittco has stated that the integration of Stittco with Gibson's Network has created the opportunity for management Synergies and more effective business systems. The Board expects to see the outcome of these synergies through reduced operating costs in the coming year. Stittco's next non-commodity cost application (expected in July of 2016) should clearly demonstrate a reduction in operating costs from these synergies. The Board expects Stittco to make every effort to control its operating costs to minimize future rate increases to customers.

Return on Rate Base

The Board agrees that Stittco should receive a reasonable return on its investment. The Board will therefore approve Stittco's rate base of \$1,971,445 and a 10% return on rate base amounting to \$197,145. The Board finds that the capital improvements to the unloading towers, at a projected cost of \$550,000, to be reasonable and warranted to meet regulation for fall protection and improved safety for rail car connection.

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.

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, 2015, **BE AND ARE HEREBY APPROVED.**
2. Stittco Utilities Manitoba Ltd's rate base of \$1,971,455 for 2015 **BE AND IS HEREBY APPROVED.**
3. All interim ex parte orders referenced in Board Orders 118/14, 9/15, 42/15 and 78/15 **BE AND ARE HEREBY APPROVED AS FINAL.**

THE PUBLIC UTILITIES BOARD

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

"Kurt Simonsen"
Acting Secretary

Certified a true copy of Order No. 106/15
issued by The Public Utilities Board

Acting Secretary

SCHEDULE " A "

GENERAL SERVICE RATE STRUCTURE
EFFECTIVE FOR CONSUMPTION ON OR AFTER NOVEMBER 1, 2015

Basic Monthly Charge	\$10.00
Volumetric Charges per m³:	
Commodity Cost Recovery	\$0.4646*
Non-Commodity Cost Recovery-Delivery Charge (monthly volumes):	
first 100 m ³	\$1.40555
next 400 m ³	\$1.25358
next 1000 m ³	\$1.18618
next 2500 m ³	\$0.96097
over 4000 m ³	\$0.73723

* Commodity Cost approved per Board Order 107/15