

1999-5

AN ORDER IN THE MATTER OF the Public Utilities Act  
Revised Statutes, 1986, c. 143, as amended

and

A Yukon Energy Corporation Application to Finalize Rates

**BEFORE:** B. Morris, Chair )  
D. Schmekel, Member )  
W. Shanks, Member ) November 10, 1999

**ORDER 1999-5**

**WHEREAS:**

- A. On December 16, 1997, Yukon Energy Corporation ("YEC") and Yukon Electrical Company Limited ("YECL") (the "Companies"), in accordance with Board Orders, filed an application to finalize 1997 rates (the "Final Rates Application"), requesting further rate riders and orders to address ongoing uncertainties related to the Faro mine operations.
- B. On April 22, 1998, YEC filed a Revised Application (the "Revised Application") requesting Board orders to finalize 1997 rates pursuant to Board Order 1997-6, approve an interim and refundable rate rider, effective for all billings on or after June 1, 1998 and other matters in the Companies' December 16, 1997 Applications.
- C. Board Order 1998-3 approved a limited scope review to facilitate an early public hearing date and set down a public hearing on the Applications to commence July 8, 1998.
- D. Board Order 1998-5 confirmed YEC's rates for 1997 as final and approved the recovery of revenue shortfalls detailed in Exhibit 83, Schedule 6D, except for recovery of the \$3,177,200 Anvil bad debt. To enable this, the Board approved interim refundable riders to be applied to the base rates for all classes of service, other than Rate Schedule 39, effective for billings issued on or after August 1, 1998. Such riders were subject to further adjustment as directed by the Board in future proceedings.
- E. The Board then directed that YEC's 1998 cost of service deduct alleged savings attributed to YECL, setting the rider at 15.28%. If the savings did not arise, the Board stated that YEC could make application to recover the greater shortfall in its application for final 1998 rates.
- F. On April 21, 1999 the Board informed YEC that it had reviewed YECL's forecasts and operations and found that any alleged cost savings were likely to be offset by other costs.

G. On August 27, 1999 YEC filed an Application to finalize its rates and to recover the \$1.6 million shortfall by way of a 3.46% increase in Rider J.

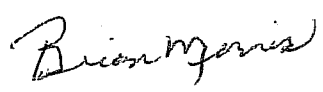
H. The Board requested and received comments from intervenors.

**NOW THEREFORE** the Board orders that:

YEC's rates are confirmed as final by way of a 3.46% increase, effective December 1, 1999, in the 15.28% rider approved by Order 1998-5, subject to YEC not filing for a further rate increase for the year ending December 31, 2000.

Dated at the City of Whitehorse, in the Yukon Territory, this 10<sup>th</sup> day of November, 1999.

**BY ORDER**



Brian Morris  
Chair

**YEC Rates Finalization Application**

**1996/97 GRA**

The last General Rate Application by the Companies was heard by the Yukon Utilities Board (the "Board") at a public hearing on March 18 and 19, 1996. The issues on which all parties could agree were enclosed in a Negotiated Settlement Package and submitted for the Board's consideration. Board Order 1996-6 approved the settlement package and the revenue requirement of the Companies, and the subsequently approved rates resulted in large decreases for Commercial, Municipal and Government customers. Residential rates did not increase despite the fact that these rates paid only 80% of the costs to serve the residential class (only 72% of the full cost after rate relief).

However, the forecasts used in the 1996/97 General Rate Application assumed that the Anvil Range Mining Corporation ("Anvil") would continue to be a Rate Schedule 39 customer of YEC providing annual revenues of almost \$15 million to cover its share of the cost of utility service. As of January 31, 1998, Anvil shut down its mining and milling operations at the Faro mine, leaving behind bad debts of \$3.2 million, a 1997 cost of service shortfall of \$1.6 million, and a 1998 shortfall in excess of \$3 million.

**The Revised Application**

On April 22, 1998, YEC filed Exhibit 19 (the "Revised Application") requesting a 16.33% rate increase. This application was based on the revenues and costs for YEC and YECL that were adopted in the Settlement Package approved by the intervenors and the Board. Board Order 1998-3 agreed that this approach was reasonable and approved a limited scope review to consider the impact of the Faro Mine shutdown. A public hearing was held on July 8, 1998.

The Board concluded that YECL's rates as approved by Board Order 1996-8 were confirmed as final in accordance with its December 16, 1997 Final Rates Application and, as a result, YECL was excused as an Applicant to the July 8, 1998 hearing.

In order to keep the immediate impact of the rate increase down, the Revised Application spread the recovery of YEC's 1997, 1998 and 1999 revenue shortfalls through rate riders and amortizations over periods of up to five years. The Revised Application further requested that interim refundable contributions be approved from the Diesel Contingency Fund to non-governmental residential and commercial customers as required to reduce the initial impact for these customers to 8.17%. The rates would be increased over time and the full impact would not immediately be felt.

**Board Order 1998-5**

Board Order 1998-5 confirmed YEC's rates for 1997 as final and approved the recovery of revenue shortfalls detailed in Exhibit 83, Schedule 6D, except for recovery of the \$3,177,200 Anvil bad debt. To enable this, the Board approved interim refundable riders to be applied to the

base rates for all classes of service, other than Rate Schedule 39, effective for billings issued on or after August 1, 1998. Such riders were subject to further adjustment as directed by the Board in future proceedings.

YEC objected to the Board's determination that the Anvil bad debt should be absorbed by YEC rather than recovered from ratepayers and filed a Notice of Application for Leave to Appeal to the Yukon Court of Appeal, pursuant to section 69 of the Public Utilities Act. This Appeal is still before the Courts.

The Revised Application had attempted to lower the rate increase impact by requesting that the fair rates of return on equity for both YEC and YECL be reduced and by assuming certain cost savings on behalf of YECL, arguing that both utilities must be treated in the same manner. The Board accepted that YECL's approved return on equity should not be changed by an application made by YEC but agreed that it could monitor YECL's forecasts and operations to satisfy itself as to whether there were cost savings to YECL not offset by other costs. The Board then directed that YEC's 1998 cost of service deduct the alleged savings attributed to YECL, setting the rider at 15.28%. If the savings did not arise, the Board stated that YEC could make application to recover the greater shortfall in its application for final 1998 rates.

### **Final Rates Application**

On April 21, 1999 the Board informed YEC that it had reviewed YECL's forecasts and operations and found that any alleged cost savings were likely to be offset by other costs, reaffirming that it would accept an Application from YEC to recover the \$1.6 million shortfall by way of a 3.46% increase in Rider J, as outlined by YEC in Schedule A (section c) of its August 31, 1998 letter to the Board. In support of this Application, and to ensure that YEC's actual return did not exceed approved levels, YEC was directed to include its 1998 Annual Report to the Board together with a forecast for 1999 similar to the information provided to the Board by YECL and forwarded to YEC for comment.

YEC filed the above Application together with supporting information ("Final Rates Application") on August 27, 1999, with copies to all intervenors. On September 30, 1999 the Utility confirmed that, subject to finalization of YEC's rates at the level applied for, YEC did not intend to file a general rate application for 2000. Intervenors were given an opportunity to comment on the Application material and responses were received from YECL, the Association of Yukon Communities ("AYC") and the Utilities Consumers' Group ("UCG").

YECL and AYC note similar concerns, namely that YEC should have renegotiated its debt with its parent, Yukon Development Corporation ("YDC"), at a lower rate of interest, that the reduced load caused by the Faro Mine shutdown should have reduced costs, and that YEC made capital expenditures in 1997 and 1998, not foreseen in the GRA.

The Board agrees (as does YEC) that utilities should examine all opportunities for refinancing existing debt at lower levels of interest. However, the issue of the appropriate level of debt and equity for a crown corporation has been examined and re-examined in previous hearings. The

General Rate Application supported by the Negotiated Settlement Package and Board Order 1996-6 noted that YEC maintains a 60:40 debt-equity ratio at an embedded cost and that all new loans from YDC will be fixed at 120 basis points above the average of long-term Government of Canada bonds as of September 30. The Board believes that the responses to UCG-YEC-1-35 and YECL-YEC-1-18 adequately explain the existing situation and YEC's ability to refinance.

YECL states that a review of City-YEC/YECL-1-7 from the 1996/97 GRA suggests there may be additional potential savings of \$597,000 over the period 1998-1999 directly related to the lower load. The additional savings is the sum of the three O & M categories shown on YECL's Appendix I for 1998 and 1999. This is comprised of Diesel O & M of about \$150,000 per year; Transmission O & M of around \$100,000 per year and General O & M of \$50,000 per year.

The \$150,000 of additional Diesel O & M savings per year arises because YECL believes that the rate per kW.h to be applied to the "lost" sales is 1.79¢ and not the 1.6¢ that YEC has used. The 1.6¢ is the incremental (marginal or variable) rate used in the Diesel Contingency Fund and a reasonable proxy for valuing the incremental savings resulting from "lost" sales. YEC says that the 1.79¢ per kW.h is in fact the average cost, which includes both fixed costs and costs that vary with sales. What needs to be done is to "back-out" the costs as those costs were "built-in" to the rates and Diesel Contingency Fund. According to YEC, 1.6¢ per kWh was added to the cost of service for each kW.h sold, so it is this number that needs to be backed-out. To the extent that additional fixed costs were "built-in" to the rates to serve the Faro Mine sales, it could be argued that those costs should also be "backed-out". It is also a reasonable argument to suggest that those fixed costs will remain basically unchanged for the near term.

YECL suggests that some \$150,000 savings in variable O & M should accrue in the annual Transmission and SCADA/telecommunications accounts. Comparing the Exhibit 83 cost adjustment forecasts, with actual 1998 and forecast 1999 results shows that the net decrease in these costs over 1998 and 1999 is closer to \$100,000, or approximately \$50,000 per year. This conclusion is drawn from YEC's "Table A2: Update to CITY-YEC/YECL-1-7 page 3". It is not evident the extent to which these costs vary in the short-run with sales volume, or what costs were "built-in" on account of the Faro sales and the potential for physically "backing-out" those costs.

YEC believes that, in addition to the lost sales from the Faro Mine itself, it will experience a further resulting loss of sales in both the residential and commercial customer classes. A lower level of economic activity represented by the loss of the Faro Mine sales, if not offset by other changes, could result in further sales losses.

On balance, the YECL submission has asked good questions and YEC has provided reasonable responses. The Board believes that there is not sufficient evidence to support additional savings in the magnitude of \$300,000 per year, considering also the additional possibility of offsetting lost contributions from residential and commercial sales. The fact is that YEC's reported actual return on equity in 1998 is 9.11%, compared to the 9.138% approved in Board Order 1998-5 and the 1999 forecast return is 8.97%.

YEC's financial statements indicate that it made capital expenditures on buildings, transportation and betterments of almost \$3 million between 1997 and 1998. YEC provided additional information on the capital expenditures questioned by YECL/AYC, asserting that the extent to which they will be recorded in rate base remains subject to further clarification and amendment and that the remainder were required in order to carry on operation of the utility.

YECL/AYC suggest that the capital expenditures may be one of the rate drivers contributing to the proposed rate increase. However, since the Utility's request is to finalize rates at 1997 levels, only adjusting for the impacts of the Faro Mine shutdown, the subsequent expenditures could not be one of the rate drivers. In fact, YEC points out that the Utility reduced its planned and approved capital program and that its net book value at the end of 1998 is actually less than the Settlement made provision for at the end of 1997. Due to the limited scope nature of the Application, the Board is not required at this time to determine whether capital expenditures made by YEC after the 1996/97 GRA were prudent.

UCG's October 25, 1999 submission states that it remains committed to a public review process. Previous letters requested that the Board order the utilities to file a General Rate Application for 1999/2000 covering 1998 as well or to "impose a rate of return (from January 1998 until a hearing decision) on the Companies that is suitable for the economic conditions of this time." The submission noted some specific issues which YEC responded to in its November 5, 1999 letter, noting that there is no impact on the current Application. Both AYC and UCG have argued that YEC's approved return on equity is too high.

Wishing to keep the rate impacts down, and recognizing that obtaining expert evidence would be time-consuming and costly, Yukon Energy Corporation was willing to adopt a lower return on equity than that approved in the 1996 hearing. Subsequent information provided by the Yukon Electrical Company Limited showed that its return was also expected to be lower than that approved. As UCG noted, Government of Canada bond yields are lower, but this is not necessarily the only determinant of a fair return. The return on equity negotiated and approved in the last hearing was 11.25%, but it should be remembered that the expert evidence submitted in the original General Rate Application, supported a return of 13.25%.

The Board recognizes that public hearings can be an extremely costly form of regulation to all parties. Both utilities' rates were set after a full public review in 1996. The subsequent limited scope hearing in July 1998 and this Order recognize that those rates were to be increased only to deal with the huge losses associated with the closure of the Faro mine, utilizing the evidence examined in the 1996 hearing.

**YUKON UTILITIES BOARD**

**P.O. Box 6070, 19 - 1114 First Avenue,**

**Whitehorse, Yukon Y1A 5L7**

**Telephone (403) 667-5058, Fax (403) 667-5059**

**Our file no.: 2210**

**Your file no.:**

November 11, 1999

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Yukon Energy Corporation  
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Y1A 5L7

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Yukon Electrical Co. Ltd.  
P.O. Box 4190  
Whitehorse, Yukon  
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Dear Sirs:

**Re: Board Order 1999 - 5**

I enclose a copy of Board Order 1999-5 finalizing Yukon Energy Corporation's 1998 rates.

Yours truly,



Jim Slater  
Board Secretary

Enclosure

cc	L. Bagnell	Association of Yukon Communities
	J. McLaughlin	AYC Energy Committee
	G. Everitt	Town of the City of Dawson City
	R. Clarkson	New Era Engineering Corp.
	R. Rondeau	Utilities Consumers' Group
	B. Newell	City of Whitehorse
	P. Percival	
	F. Roberts	
	P McMahan	YTG Dept. of Economic Development