

**IN THE MATTER OF YUKON
ELECTRICAL COMPANY
LIMITED 2016-2017
GENERAL RATE APPLICATION**

**FINAL ARGUMENT
YUKON ENERGY CORPORATION**

November 24, 2016

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1.0 INTRODUCTION

Yukon Energy Corporation (Yukon Energy or YEC) intervened and participated in the Yukon Electrical Company Limited (Yukon Electrical, YECL, or AEY) 2016-17 General Rate Application proceeding.

As the primary generator and transmitter of electricity on the integrated system in Yukon, and also as a distributor, Yukon Energy has a material interest in the outcome of YECL's Application. Yukon Energy's intervention focused primarily on issues relevant to the integrated grid system (e.g. load forecasts affecting YEC wholesales [YECL purchase power requirements], Fish Lake expected generation, planning for future generation projects on the grid), and on matters that are jointly of interest to Yukon Energy and Yukon Electrical in the context of decisions by the Yukon Utilities Board (YUB or Board) on the Application setting precedents that may potentially affect future YEC revenue requirement applications (e.g. return on equity determinations and Rider F).

Yukon Energy does not in Argument propose to address all matters covered in YECL's Application, information requests or oral evidence; however, the failure of YEC to address any specific matter should not be interpreted as concurrence with YECL's position, and Yukon Energy expressly reserves its right to address all matters in Reply Argument if the need arises.

Yukon Energy in Argument limits its submissions and comments at this time to review of appropriateness of the requested ROE and equity share of capital structure for the utility based on past precedents in Yukon applicable to YUB regulation of Yukon Energy and Yukon Electrical.

2.0 RETURN ON EQUITY & CAPITAL STRUCTURE

Yukon Electrical is requesting a return on equity (ROE) for the 2016-2017 test period linked to the recently approved British Columbia Utilities Commission (BCUC) Generic Cost of Capital (GCOC) benchmark rate of 8.75% plus a risk premium of 0.60% (total requested ROE of 9.23%). Notably, the requested risk premium of 0.60% over the BCUC GCOC benchmark return on equity is higher than the risk premium of 0.46% previously approved by the Board for YECL in Order 2009-2¹. This is also higher than the risk premium of 0.52% previously approved by the Board for YEC in Order 2005-12 and Order 2008-9.

YECL engaged Concentric Energy Advisors, Inc. (Concentric) to determine whether a risk premium relative to the BCUC GCOC benchmark utility would be appropriate and if so what that risk premium should be. The report provided by Concentric concluded as follows regarding the risk premium for YECL²:

- "A risk premium between 40 and 75 basis points is appropriate for AEY as compared to the BCUC benchmark utility." The range is framed by FortisBC Electric on the lower end and PNG-West on the upper end in relation to the benchmark.

¹ Order 2009-2, page 29.

² AEY Application, Attachment 8.1, page 6.

- Concentric concluded that a risk premium for AEY of 60 basis points is reasonable because it would be consistent with the recent 9.35% ROE award for Maritime Electric, a company with similar business risk as AEY and a deemed equity ratio of 40.9%.

2.1 ISSUES AND CONCERNS WITH YECL'S APPROACH TO DETERMINING FAIR ROE

Yukon Energy agrees that it is appropriate to use the BCUC Benchmark ROE of 8.75% as the foundation to determining a fair return on equity for the test years, and that for Yukon utilities it is appropriate to apply a risk premium adder above the benchmark in order to reflect additional risks faced by northern utilities on an isolated grid.

However, Yukon Energy is concerned about the approach used by Yukon Electrical to determine the quantum of the risk premium adder. Specifically, Yukon Energy is concerned that the proposed approach deviates from the BCUC approach and from past Yukon precedent, and also maintains a requirement for expert evidence and testimony to determine return on equity for Yukon utilities, potentially increasing both the cost and complexity of these proceedings.

The following key issues are noted regarding Yukon Electrical's approach to determining return on equity:

1. **A more simplified approach that reduces regulatory costs and complexity has been used and accepted by the Board in the past:** The Board has consistently noted that it "continues to be of the view that relying on a generic ROE from a different jurisdiction is the most efficient means of addressing an inherently complex and costly matter," and "strongly believes that such an approach is the most efficient manner for a jurisdiction such as Yukon."³ In addition to approving use of simplified approaches that rely on a benchmark ROE established by another regulator (typically BCUC), the Board has also approved using the following simplified approach to determining the risk premium adder to be applied to the benchmark ROE adopted.
 - a. Order 2005-12 approved use of a simplified approach for determining YEC's risk premium adder that was based on the midway point between two BCUC comparator utilities: FortisBC Electric (40 basis points) and PNG-West (65 basis points). It was accepted at the time that Yukon Energy was less risky than PNG, but more risky than FortisBC Electric due to the fact that FortisBC Electric had interconnections with other utilities and could purchase more of its demand when required.⁴ The Board also noted "to ensure that there is sufficient forecast risk within the revenue requirement model, YEC should be at risk for their forecasts of load, OM&A and capital expenditures."⁵ This approach relied on providing comparative information for these BCUC comparator utilities, and did not require expert evidence to determine the risk premium adder. Order 2008-9, reaffirmed the use of the BCUC benchmark ROE as a precedent for Yukon and accepted the risk premium of 52 basis points previously established for YEC in Order 2005-12.

³ Order 2009-8, page 53-54.

⁴ Order 2005-12, Appendix A, page 44 and 45.

⁵ Order 2005-12, Appendix A, page 45.

- b. Order 2009-2, also approved use of this simplified approach for determining the risk premium adder relative to the BCUC benchmark ROE for YECL. The Board concluded that it was reasonable to place the risk premium for YECL at the midpoint of the risk premiums between Yukon Energy (52 basis points) and FortisBC Electric (40 basis points), noting YECL's acknowledgement that "relative to YECL, YEC has more risk" and "without the same inter-tie connections as FortisBC, YECL is more risky than FortisBC."⁶

The above approach applied to the updated evidence on BCUC risk premium decisions, as provided in the current YECL proceeding, would result in a risk premium adder for Yukon Energy of 57.5 basis points (midway between FortisBC Electric and PNG-West), and for Yukon Electrical of 48.5 basis points (midway between Yukon Energy and FortisBC Electric).

2. **The approach adopted by YECL deviates from the simplified approach used in the past to reduce regulatory costs and complexity** – The approach used in Yukon Electrical's Application ultimately focuses on expert testimony regarding YECL's business risks relative to a number of gas and electric distribution utilities across Canada,⁷ and a conclusion that Maritime Electric's ROE is an appropriate comparator for Yukon Electrical. This approach deviates from the simplified approach used in 2005 and in 2008/09 which relied on comparison to two BC Comparator utilities (FortisBC Electric and PNG-West), and which did not require expert business risk analysis and reviews of economic and capital market conditions.

Prior Board directions have indicated a preference to maintain consistency with an approach used in a single jurisdiction; however, the approach adopted by Yukon Electrical focuses on review of comparator utilities outside of Yukon and BC (i.e., Newfoundland Power and Maritime Electric) to justify the risk premium adder.

Specifically, the recommended risk premium adder of 60 basis points is supported in the Application based on a comparison with Maritime Electric which Concentric asserts has a similar business risk to YECL, a deemed equity ratio of 40.9% and an approved ROE of 9.35%. Using this approach, the 60 basis point adder is simply the difference required to achieve a 9.35% ROE, and the assessment mainly relies on comparison to Maritime Electric to justify the overall ROE. In this context, the BCUC benchmark and BCUC comparator utilities do not materially inform the ROE determination or risk premium adder determination at all.

3. **The approach adopted results in a material increase in the risk premium adder for Yukon utilities compared to prior Yukon reviews** (Order 2005-12, Order 2009-2 and Order 2009-8) – Yukon Electrical's approach results in an increase in risk premium for YECL from 46 basis points to 60 basis points despite the finding in the Concentric Report that there has not

⁶ Order 2009-2, page 29.

⁷ Comparator utilities included in the assessment are summarized in pages 4 to 6 of the Concentric Report and include: FortisBC Energy, FortisBC Electric, Newfoundland Power, Maritime Electric, ATCO Electric Distribution and PNG-West.

been a material change in business risk for YECL since this was last assessed in detail in 2009. Specifically, the Concentric Report concludes that “in most respects, AEY’s business risk has not materially changed since 2009 when the Board determined that a risk premium of 46 basis points above the benchmark utility in British Columbia was reasonable.”⁸ This conclusion was provided while noting changes for YECL related to uncertainty and unpredictability associated with UPC among residential class driven by fuel switching, DSM programs and downturn in economic conditions over the past three years which have made it more difficult for YECL to accurately forecast sales.

Accepting Yukon Electrical's risk premium of 60 basis points would also mean by implication, based on all past evidence and precedents, that YEC would now require a risk premium greater than 60 basis points.

2.2 CONCLUSIONS & RECOMMENDATION

It is recommended that the Board continue to use the same methodology and justification for determining Fair ROE that was established for the 2005 GRA and used and accepted by the Board in the 2008/09 GRA. This approach relies solely on information from a single external jurisdiction (BCUC) for both the benchmark ROE and the appropriate risk premium adder for both YEC and YECL. Based on the evidence in the current proceeding, the BCUC benchmark ROE is 8.75% and the applicable risk premium adders are 57.5 basis points for Yukon Energy (midway between FortisBC Electric and PNG-West), and 48.5 basis points for Yukon Electrical (midway between Yukon Energy and FortisBC Electric).

⁸ AEY Application, Attachment 8.1, page 31.