

2002-3

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

And

**Yukon Energy Corporation and The Yukon Electrical Company
Limited
Diesel Contingency Fund/Fire Reports**

BEFORE: B. Morris, Chair)
 W. Shanks, Vice-Chair)
 G. Leslie)
 R. Hancock)
 M. Phillips) November 6, 2002

ORDER 2002-3

WHEREAS:

- A. The terms of the 1996/97 Negotiated Settlement approved by Board Order 1996-6 provided for the creation of a Diesel Contingency Fund ("DCF") to smooth customer rate changes and offset forecast diesel costs.
- B. The terms also provided that an annual report detailing additions and deletions to the fund is to be filed with the Board so that the Board may oversee the fund activities.
- C. On April 20, 2000 Yukon Energy Corporation ("YEC") filed a report, detailing the changes to the Diesel Contingency Fund in 1999, requesting that it be approved as filed.
- D. The Board provided interested parties with an opportunity to comment on the report and issues were raised with respect to the impact of the October 1997 fire at the Whitehorse Rapids Generating Station which could not be resolved until YEC completed its negotiations with its insurance companies.
- E. On October 6, 2000 the Board acknowledged that it would not make a determination on the additions and deletions to the 1999 DCF until further notice.
- F. On August 17, 2001 YEC filed a report on the operation of the DCF in 2000, noting that there was no activity impacting the fund other than interest and service fees, and requesting that it be approved as filed.
- G. On April 26, 2002 YEC reported that it had reached a settlement with its insurance companies and filed a final report on the impacts relating to the fire at the Whitehorse Rapids Generating Station ("Fire Report").

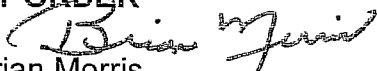
- H. YEC requested an Order that, with the filing of the Fire Report, it has complied with the reporting requirements directed by the Board and that an insurance gain of \$744,000 be placed into a deferral account for the benefit of ratepayers pending further direction of the Board. YEC also requested an Order approving that the December 31, 2000 DCF balance be changed as outlined in Section IV of the Fire Report.
- I. On May 27, 2002 the Board provided interested parties with an opportunity to comment.
- J. After a series of information requests to YEC, the Utilities Consumers' Group and The Yukon Electrical Company Limited provided their comments, to which YEC replied on September 3, 2002.
- K. The Board has reviewed the material.

NOW THEREFORE, for the Reasons attached as Appendix A, the Board orders that:

1. YEC has complied with the reporting requirements directed by the Board relating to the October 1997 fire.
2. The insurance gain of \$744,000 realized as part of the settlement of the insurance claim arising from the fire is to be placed into a deferral account as an offset to rate base for the benefit of ratepayers pending further direction of the Board.
3. The additions and deletions to the Diesel Contingency Fund for 1999 and 2000 are approved as filed, except that the December 31, 2000 balance is to be changed from (\$61,744.29) to \$681,721.92 as outlined in section IV of the Fire Report.

Dated at the City of Whitehorse, in the Yukon Territory, this 6th day of November 2002.

BY ORDER


Brian Morris
Chair

**YUKON ENERGY CORPORATION
DIESEL CONTINGENCY FUND AND FIRE REPORTS**

Diesel Contingency Fund Reports

The terms of the 1996/97 Negotiated Settlement approved by Board Order 1996-6 provided for the creation of a Diesel Contingency Fund ("DCF") to smooth customer rate changes and offset forecast diesel costs. The settlement terms also provided that an annual report detailing additions and deletions to the fund is to be filed with the Board so that the Board may oversee the fund activities. The fund is intended to offset diesel generation cost changes for the Whitehorse Rapids/Aishihik/Faro ("WAF") system that are caused solely by variances from long term average levels of WAF system hydro and wind generation, although the Board has approved its use to mitigate the rate impact of the Faro Mine shutdown.

On June 2, 1999 Yukon Energy Corporation ("YEC") filed a report, detailing the changes to the Diesel Contingency Fund in 1998, together with revised reports for 1996 and 1997. YEC reported that actual diesel generation was required during three months of 1997 due to reduced hydro capability caused by the October 1997 fire at the Whitehorse Rapids Generating Station. However, the report noted that the DCF drawdowns had been charged to the Corporation's Reserve Fund and the fire insurance claim. Board Order 1999-3 subsequently approved the additions and deletions to the DCF for the period 1996-1998.

On April 20, 2000 YEC filed a report, detailing the changes to the Diesel Contingency Fund in 1999, requesting that it be approved as filed. Before making its determination, the Board provided interested parties with the opportunity to comment. During this period, YEC responded to Information Requests from The Yukon Electrical Company Limited ("YECL") concerning the impacts of the 1997 fire on the DCF in 1999. Essentially, YECL requested confirmation that, due to the fire, Whitehorse Rapids hydro production was lost from October 30, 1997 to late 1998. In order to meet the load, YEC used stored water at Aishihik Lake. However, Aishihik did not refill to capacity in 1999 and, as a result, YEC would have burned diesel fuel to meet loads in 1999 that otherwise would have been met by Aishihik water. If so, the cost of such diesel fuel should not be considered a valid drawdown item for the DCF.

In an October 4, 2000 letter to the Board, YEC stated that its legal counsel had advised that, given the status of the negotiations, it would be premature and potentially prejudicial to estimate what amounts might be recovered in relation to these issues, and that it would provide a full report to the Board once the negotiations are completed. By letter of October 6, 2000, the Board informed all stakeholders that it would defer any determination on the additions and deletions to the 1999 DCF until further notice.

On August 17, 2001 YEC filed DCF schedules and tables for 2000, noting that there was no activity other than monthly interest and account service fees, and requesting that the Board approve it as filed. As there were no additions and deletions, the Board took no action, awaiting receipt of the Fire Report. As filed, the 2000 DCF had a yearend debit balance of \$61,744.29.

On April 26, 2002 YEC reported that it had reached a settlement with its insurance companies and filed a final report on the fire impacts ("Fire Report"). YEC requested an Order that, with the filing of the Fire Report, it has complied with the reporting requirements directed by the Board and that an insurance gain of \$744,000 be placed into a deferral account for the benefit of ratepayers pending further direction of the Board. YEC also requested an Order approving that the December 31, 2000 DCF balance be changed as outlined in Section IV of the Fire Report.

The Fire Report addressed the 1999 DCF fire-related impacts, recognizing that Aishihik was used in 1998 to generate power to offset fire-related generation losses. With Aishihik Lake at a low supply level, diesel generation was required and initially charged to the DCF in January, February, April, May, November and December of 1999. YEC's best estimate was that the water level at Aishihik Lake at the end of 1998 was about 13 cm. lower than it would have been but for the fire, and equated this to 7-8 GW.h of generating capability. As this was approximately the amount of diesel generation in January and February 1999, YEC credited the DCF with the amounts originally charged, totaling \$674,413.21.

On May 27, 2002 the Board provided interested parties with an opportunity to comment. and, after a series of information requests to YEC, the Utilities Consumers' Group and The Yukon Electrical Company Limited provided their comments, to which YEC replied on September 3, 2002.

The Utilities Consumers' Group suggested that the total drawdown of the DCF for 1999 should be replaced in the DCF balance, believing that it was diesel burned during restoration of equipment caused by the fire. The Utilities Consumers' Group also submitted that the diesel generation expense of \$281,000 should be placed in the DCF. YEC replied that all expenses related to the fire have been accounted for in the DCF.

The Yukon Electrical Company Limited submitted that a calculation consistent with an April 6, 1998 letter from YEC/YECL would translate into a lost generating capability of 7,893,333 kW.h and that another \$90,214.58 should be added to the DCF balance. YEC replied that such a level of exactness is not appropriate or necessary in the circumstances, reiterating that any change would only result in a reallocation of the total \$1.4 million gain from one pocket to the other.

The Board agrees that YEC's calculations are a reasonable representation of the impacts of the fire on the DCF. The additions and deletions to the Diesel Contingency Fund for 1999 and 2000 are approved as filed, except that the December 31, 2000 balance is to be changed from (\$61, 744.29) to \$681,721.92 as outlined in section IV of the Fire Report.

Fire Report

The October 1997 fire completely destroyed three of the four turbines at the dam, the automated control system for the WAF grid, and the YEC headquarters. In a June 26, 1998 status report to the Board, YEC stated that it had both property loss insurance, which would be used to replace the destroyed assets, and compensation insurance for loss of hydro generation production. The Corporation expected that there will be no implications from the 1997 fire for its costs or earnings in 1998 or subsequent years, but stated that it could address these matters only when complete information is available.

On May 25, 2000 YEC reported that the replacement of the destroyed assets with equivalent new assets had resulted in a positive variance between the property loss insurance receivable and the net book value of the destroyed assets. The Auditor General advised YEC that, in the absence of any direction from the Yukon Utilities Board, Generally Accepted Accounting Principles ("GAAP") would require YEC to record the fire insurance gains as income for YEC in 1999. The effect of this treatment would be to cause the gain to accrue to YEC's shareholder. Also, the higher depreciation on the purchase price of the replacement assets would result in an increased revenue requirement from ratepayers. YEC therefore requested and received approval (Board Order 2000-3) to vary from GAAP to ensure the gain is assigned to the benefit of ratepayers.

The April 26, 2002 Fire Report noted that, of the total \$14,518,932.44 settlement amount, \$13,031,000 was related to the cost of replacement assets, additional O&M, and refurbishment of the insurance reserve, leaving \$1,488,000 in surplus proceeds. Of this amount, \$744,000 was determined to be the appropriate adjustment to the 1999 DCF fire-related impacts, leaving an unallocated gain of \$744,000 which YEC placed into a deferral account. In its response to an information request, YEC stated that eventually the funds could be used to offset increases in insurance premiums or deductibles.

The Yukon Electrical Company Limited submitted to the Board that, while it believed that YEC has complied with the Board's reporting requirements, the deferred insurance gain should not be included in YEC's rate base calculation and that all investment income earned on the proceeds of the insurance gain should go to the deferral account rather than YEC's investment income. The Utilities Consumers' Group was concerned about the accountability of any deferral accounts.

YEC replied that the disposition of funds from all deferral accounts is subject to Board review and approval, and that the use of offsets to rate base are normal utility practices eliminating the need for administrative fees. YEC states that it does not earn investment interest on the insurance funds and points out that the benefit to ratepayers is the equivalent of the full weighted average cost of capital of the utility, which is well in excess of the interest rate on externally invested funds.

The Board agrees with YEC and directs that the insurance gain of \$744,000 realized as part of the settlement of the insurance claim arising from the fire is to be placed into a deferral account for the benefit of ratepayers, pending further direction of the Board. YEC has complied with the reporting requirements directed by the Board relating to the October 1997 fire.