YUKON DEVELOPMENT CORPORATION

FINANCIAL STATEMENTS

December 31, 2011

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Yukon Development Corporation

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The consolidated financial statements of Yukon Development Corporation are the responsibility of management, and have been prepared in accordance with Canadian generally accepted accounting principles consistently applied and appropriate in the circumstances. The preparation of financial statements necessarily involves the use of estimates and approximations, which have been made using careful judgement. In management's opinion, the consolidated financial statements have been properly prepared within reasonable limits of materiality and within the framework of the accounting policies summarized in the consolidated financial statements.

Management maintains systems of internal controls designed to provide reasonable assurance that assets are safeguarded and that reliable financial information is available on a timely basis. These systems include formal written policies and procedures, the careful selection and training of qualified personnel, and an organizational structure that provides for the appropriate delegation of authority and segregation of responsibilities.

The financial statements have been examined by an independent external auditor. The external auditor's responsibility is to express an opinion on whether the consolidated financial statements, in all material respects, fairly present the Corporation's financial position, results of operations and cash flows in accordance with Canadian generally accepted accounting principles. In addition, the external auditor reports on whether proper books of account have been kept by the Corporation, the consolidated financial statements are in agreement therewith, and the transactions coming to their notice have, in all significant respects, been in accordance with specified authorities. The Auditor's Report, which follows, outlines the scope of this examination and the auditor's opinion.

The Corporation's Board of Directors, through its Audit and Finance Committee, oversees management's responsibilities for financial reporting. The Audit and Finance Committee meets with management and the independent external auditor to discuss auditing and financial matters, to gain assurance that management is carrying out its responsibilities and to review and approve the consolidated financial statements. The auditor has full and free access to the Audit and Finance Committee, with and without the presence of management.

David Morrison
Chief Executive Officer

Blaine Anderson, C.A.
Chief Financial Officer

Whitehorse, Yukon
May 10, 2012

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Auditor General of Canada
Vérificateur général du Canada

INDEPENDENT AUDITOR'S REPORT

To the Minister Responsible for Yukon Development Corporation

Report on the Consolidated Financial Statements

I have audited the accompanying consolidated financial statements of Yukon Development Corporation, which comprise the consolidated balance sheet as at 31 December 2011, and the consolidated statement of operations, comprehensive income and retained earnings and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

My responsibility is to express an opinion on these consolidated financial statements based on my audit. I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

In my opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Yukon Development Corporation as at 31 December 2011, and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

240 rue Sparks Street, Ottawa, Ontario K1A 0G6

Report on Other Legal and Regulatory Requirements

As required by the *Yukon Development Corporation Act,* I report that, in my opinion, Canadian generally accepted accounting principles have been applied on a basis consistent with that of the preceding year.

Further, in my opinion, proper books of account have been kept by Yukon Development Corporation and its wholly-owned subsidiary and the consolidated financial statements are in agreement therewith. In addition, the transactions of Yukon Development Corporation and its wholly-owned subsidiary that have come to my notice during my audit of the consolidated financial statements have, in all significant respects, been in accordance with the *Financial Administration Act* of Yukon and regulations, the *Yukon Development Act* and regulations, the *Public Utilities Act* and regulations, the *Business Corporations Act* and regulations, and the articles and by-laws of Yukon Development Corporation and its wholly-owned subsidiary.

Terrance DeJong, CA
Assistant Auditor General
for the Auditor General of Canada

10 May 2012
Edmonton, Canada

Yukon Development Corporation

Consolidated Balance Sheet

As at December 31, (in thousands of dollars)	2011	2010
### Assets		
Current assets		
Cash (note 5)	$ 8,423	$ 32,731
Accounts receivable (note 6)	25,847	29,851
Materials and supplies	2,830	2,648
Prepaid expenses	614	368
Current portion of direct financing leases (note 8)	-	413
	37,714	66,011
Customer contribution financing (note 7)	-	17,424
Direct financing leases (note 8)	**162**	162
Diesel contingency fund (note 9)	**902**	891
Property, plant and equipment (note 10)	**368,243**	281,134
Deferred uninsured losses (note 11)	**576**	432
Deferred charges and intangible assets (note 12)	**25,273**	19,007
	$ 432,870	$ 385,061
### Liabilities		
Current liabilities		
Bank indebtedness (note 13)	$ 4,782	$ -
Accounts payable and accrued liabilities (note 14)	27,472	17,335
Derivative related liability (note 25)	824	435
Current portion of long-term debt (note 16)	3,826	4,270
	36,904	22,040
Faro Mine dewatering deferral revenue (note 15)	**397**	397
Long-term pension liability (note 22)	**1,137**	1,035
Long-term debt (note 16)	**121,089**	124,810
Contributions in aid of construction (note 17)	**108,895**	75,447
Regulatory provision for future removal and site restoration costs	**4,711**	4,764
Diesel contingency fund (note 9)	**902**	891
	274,035	229,384
### Equity		
Contributed capital	**41,501**	41,501
Retained earnings	**117,334**	114,176
	158,835	155,677
	$ 432,870	$ 385,061

Commitments and Contingencies (notes 23 and 24)

The accompanying notes are an integral part of the financial statements.

Approved by the Board:

Chair **Director**

Yukon Development Corporation

Consolidated Statement of Operations, Comprehensive Income and Retained Earnings

For the year ended December 31, (in thousands of dollars)	**2011**	2010
Revenue		
Sales of power (note 18)	$ 33,782	$ 31,931
Government of Yukon (note 1)	4,357	3,029
Interest income	569	1,544
Allowance for funds used during construction	555	514
Other income	254	214
Finance income	12	92
	39,529	37,324
Expenses		
Operations and maintenance (note 19)	10,288	7,899
Administration (note 20)	9,155	8,445
Interest on long-term debt	6,267	4,180
Amortization of property, plant and equipment	5,804	5,417
Amortization of deferred charges	915	871
Amortization of intangible assets	528	548
Provision for uninsured losses (note 11)	100	100
	33,057	27,460
Net income before other items	**6,472**	9,864
Interim electrical rebate program (note 1)	**(2,926)**	(2,782)
Unrealized gain (loss) on interest rate swaps (note 26)	**(388)**	(139)
Net income	**3,158**	6,943
Other comprehensive income	**-**	-
Comprehensive income	**3,158**	6,943
Retained earnings, beginning of year	**114,176**	107,233
Retained earnings, end of year	**$ 117,334**	$ 114,176

The accompanying notes are an integral part of the financial statements.

Yukon Development Corporation

Consolidated Statement of Cash Flows

For the year ended December 31, (in thousands of dollars)	2011	2010
Operating activities		
Cash receipts from customers	$ 38,700	$ 34,060
Cash paid to employees and suppliers	(20,656)	(9,293)
Interest paid	(6,267)	(4,180)
Interest received	582	1,636
Cash provided by operating activities	**12,359**	22,223
Financing activities		
Repayment of long-term debt	(4,263)	(4,388)
Proceeds from long-term debt	98	98,169
Repayment of short-term financing	-	(25,000)
Contributions in aid of construction	38,174	9,632
Cash provided by financing activities	**34,009**	78,413
Investing activities		
Additions to property, plant and equipment	(85,840)	(79,460)
Additions to deferred charges and intangible assets	(7,456)	(6,372)
Proceeds from investments	414	760
Proceeds from long-term receivable	17,424	-
Cash used in investing activities	**(75,458)**	(85,072)
Net increase (decrease) in cash	**(29,090)**	15,564
Cash, beginning of year	**32,731**	17,167
Cash, end of year	**$ 3,641**	$ 32,731
Cash includes:		
Cash (Note 5)	$ 8,423	$ 32,731
Bank indebtedness	(4,782)	-
Total	$ 3,641	$ 32,731

The accompanying notes are an integral part of the financial statements.

1. Nature of operations

Yukon Development Corporation (the "Corporation") was originally established under the *Yukon Development Corporation Act* to participate with the private sector in the economic development of the Yukon, to make strategic investments to the benefit of the territory and to acquire and operate the assets of Northern Canada Power Commission in the Yukon. In 1993, the Corporation's mandate was changed to restrict its new initiatives to energy-related activities designed to promote the economic development of the Yukon.

The Corporation's wholly-owned subsidiary, Yukon Energy Corporation (the "Utility") was incorporated under the Yukon *Business Corporations Act*. The Utility generates, transmits, distributes and sells electrical energy in the Yukon and is subject to overall regulation by the Yukon Utilities Board (YUB) and specific regulation by the Yukon Territory Water Board. Both of these boards are independent from the Utility. The Utility is also exempt from the Financial Administration Act (Yukon).

Rate regulation
The operations of the Utility are regulated by the YUB pursuant to the *Public Utilities Act (Yukon)*. There is no minimum requirement for the Utility to appear before the YUB to review rates. However, the Utility is not permitted to charge any rate for the supply of power that is not approved by an Order of the YUB. The Utility is subject to a cost of service regulatory mechanism under which the YUB establishes the revenues required (i) to recover the forecast operating costs, including depreciation and amortization, of providing the regulated service, and (ii) to provide a fair and reasonable return on utility investment or rate base. As actual operating conditions may vary from forecast, actual returns achieved can differ from approved returns.

The regulatory hearing process used to establish or change rates typically begins when the Utility makes an application for its proposed electricity rate changes over the next one or two forecast years. The YUB must ensure that its decision, which fixes electricity rates, complies with appropriate principals of rate making, all relevant legislation including the *Public Utilities Act* and directives issued by the Yukon Government through Orders-In-Council that specify how the interests of the customer and Utility are to be balanced.

The YUB typically follows a two-stage decision process. In the first stage, the total costs that the Utility will incur to provide electricity to its customers over the immediate future are reviewed and approved. The approval of these costs determines the total revenues the Utility is allowed to collect from its customers. It is the responsibility of the YUB to examine the legitimacy of three classes of costs:

- the costs to the Utility to run its operations and maintain its equipment (personnel and materials);
- the cost associated with the amortization of all capital equipment; and
- the return on rate base (the costs related to borrowing that portion of the rate base which is financed with debt, and the costs to provide a reasonable rate of return on that portion of the rate base which is financed with equity).

The YUB assesses the prudency of costs added to rate base, which includes an allowance for funds used during construction (AFUDC) charged to capital projects. The YUB also reviews the appropriateness of asset depreciation rates, which are periodically updated by the Utility through depreciation studies.

In the second stage, the YUB approves how the revenue will be raised. This stage essentially determines the electricity rates for the various customer classes in the Yukon: residential, government, commercial and industrial. This process is guided mainly by requirements of Yukon Government Order-in Council 1995/90 and can include a cost-of-service study which allocates the overall Utility's cost of service to the various customer classes on the basis of appropriate costing principles.

Normally, the Utility applies for rates in advance of the applicable years (Note 29).

1. Nature of operations - continued

Water regulation
The Yukon Territory Water Board pursuant to the *Yukon Waters Act* decides if and for how long the Utility will have a water license for the purposes of operating hydro generation stations in the Yukon. The licenses will also indicate terms and conditions for the operation of these facilities.

Capital structure
The Utility's policy is to maintain a capital structure of 60% debt and 40% equity at year end. Annual dividends are declared to the parent and typically loaned back in order to maintain this ratio.

Government of Yukon
In May 2011, the Yukon Government authorized the continuation of the Interim Electrical Rebate program (the "rebate") for 18 months at current levels, to September 30, 2012. The rebate provides subsidies to non-government residential and municipal customers. It was implemented in 1998 after the Faro mine closed to protect customers from significant bill increases that would have resulted from that shutdown. The Yukon Government is providing funding for the rebate to a maximum of $3 million per year. In 2011, the Corporation received $3.044 million (2010 - $3.029 million) in funding for the program. The total subsidy payments made by the Corporation during the current year were $2.925 million (2010 - $2.782 million).

The Corporation and the Government of Yukon signed a Memorandum of Understanding for the accounting period starting April 1, 2011 to March 31, 2042 regarding the Mayo B and Carmacks-Stewart Transmission line projects. The Government of Yukon will assist in funding the repayment of a portion of the bond interest costs of up to $2.625 million annually, subject to the Corporation meeting specified terms set out in the agreement.

2. Accounting changes

Future accounting changes
Publically accountable enterprises are required to move from Canadian Generally Accepted Accounting Principles to International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board (IASB) and adopted by the Canadian Institute of Chartered Accountants, for years beginning on or after January 1, 2011. IFRS uses a conceptual framework similar to Canadian GAAP, but there are significant differences in recognition, measurement and disclosures.

On October 1, 2010, the Canadian Accounting Standards Board (AcSB) issued guidance to allow, but not require, entities with rate regulated activities to defer the transition. The Utility had elected to take this deferral option. In March 2012, the AcSB announced a further one year deferral for qualifying rate regulated entities to January 1, 2013. This further extension is offered in recognition that the IASB may choose to include rate regulated activities on its future agenda. The Utility has chosen to adopt this deferral and continues to monitor the situation. The deferral also applies to the consolidated financial statements of parents of qualifying entities with rate-regulated activities.

3. Significant accounting policies

Financial statement presentation
The consolidated financial statements of the Corporation have been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP") and include the accounts of Yukon Development Corporation and its wholly owned subsidiary, Yukon Energy Corporation. All significant inter-company transactions and balances have been eliminated on consolidation.

3. Significant accounting policies - continued

The consolidated financial statements reflect the rate regulated accounting policies adopted by the Utility which differ from the accounting policies otherwise expected using GAAP. In particular, the timing of the Utility's recognition of certain assets, liabilities, revenues and expenses as a result of regulation differ from that of a non-regulated enterprise. The impact on the financial statements of accounting for rate regulated operations are further described in note 4. The significant accounting policies have been classified accordingly in the notes below:

Rate regulated accounting policies adopted by the Utility

Allowance for funds used during construction
The cost of the Utility's property, plant and equipment and deferred charges includes an allowance for funds used during construction (AFUDC) as allowed by the regulator. In prior years, the AFUDC rate estimate was based on the Utility's weighted average cost of capital (which included a cost of debt component and a return on equity component). In 2011 management revised its AFUDC rate estimate to remove the return on equity component and calculated the estimate based on the Utility's weighted average cost of debt. This change in estimate was applied prospectively effective January 1, 2011. The AFUDC rate estimate was 4.483% for 2011 (2010 - 7.09%).

Property, plant and equipment
The gain or loss on the disposal or retirement of property, plant and equipment, with the exception of land and vehicles, is deferred and amortized over the remaining expected useful lives of the assets.

Faro Mine dewatering deferral revenue
Faro mine dewatering deferral revenue represents amounts ordered by the YUB to be held by the Utility on behalf of ratepayers. The YUB has sole discretion to direct disposition of these funds, typically through refunds to customers or applied to ratepayer deficits.

Deferred uninsured losses
The Utility maintains a regulatory account for recording uninsured losses. An annual provision is approved by the YUB and collected through customer rates. Variances between the approved annual provision and actual costs incurred are deferred until the following general rate application or until a specific application is made to the YUB requesting recovery from or refund to customers.

Deferred charges
Deferred charges are recorded at cost and include an AFUDC component as allowed by the regulator.

All deferred charges are amortized to earnings on a straight-line basis over terms approved by the Yukon Utilities Board.

Cost of feasibility studies and infrastructure planning which did not result in a capital project are amortized over terms raging between five and ten years.

IFRS costs are associated with the accounting conversion from Canadian Generally Accepted Accounting Principles to International Financial Reporting Standards.

Deferred customer service costs are amortized over twelve years.

The deferred hearing cost account is used to record the deferral of costs associated with preparation and defense of applications to the YUB. The periods of amortization range from 10 to 45 years.

Regulatory provision for future removal and site restoration costs
The Utility maintains a provision for the future removal of property, plant and equipment and the costs of site restoration related to those assets. Per YUB Order 2005-12 no additional provision is permitted.

December 31, 2011 (tabular amounts in thousands of dollars)

3. **Significant accounting policies - continued**

This account provides for the costs of demolishing, dismantling, tearing down, or otherwise disposing of an asset and any site restoration costs, net of actual recoveries. This account is not used when the costs relate to an asset retirement obligation.

Deferred insurance proceeds
Deferred insurance proceeds represents a gain on fire insurance proceeds received related to a fire at the Whitehorse Rapids Generating Station in 1997. The proceeds are being amortized to income on the same basis as the replacement assets.

Diesel contingency fund
The Utility maintains an asset and an offsetting liability on behalf of ratepayers. The fund is used to reimburse the Utility for costs associated with diesel generation required when there is not sufficient water for hydraulic generation to meet demand. The Utility is required to file an annual report with the YUB on the fund's activity.

Generally Accepted Accounting Principles ("GAAP") adopted by the Corporation and Utility

Revenue recognition
All revenues are recognized in the period earned. Revenue from the sale of power is recognized based on cyclical meter readings. Sales of power includes an accrual for electricity deliveries not yet billed.

Materials and supplies
Diesel fuel, materials and supplies are recorded at the lesser of average cost and net realizable value. Obsolete materials and supplies are recorded at salvage value in the period when obsolescence is determined. Major spare parts are recorded in the Utility's books as property and equipment.

Property, plant and equipment
Property, plant and equipment is stated at cost, other than the AFUDC component which is recorded under rate regulated accounting. Cost includes materials, direct labour, a proportionate share of directly attributable administration overhead, and, if applicable, direct finance charges capitalized during construction, less accumulated amortization. Amortization is based on the straight-line method over the estimated economic life of the assets as follows:

Generation	
Hydro-electric plants	30 to 65 years
Diesel plants	25 to 45 years
Wind turbines	30 years
Transmission	40 to 50 years
Distribution	30 to 40 years
Buildings	20 to 40 years
Financial Information System	5 to 10 years
Transportation	9 to 31 years
Other equipment	5 to 20 years

Asset retirement obligations
On an annual basis the Utility identifies legal obligations associated with the retirement of tangible long-lived assets. Where a reasonable estimate of the fair value of these obligations can be determined, the total retirement costs are to be recorded as a liability at fair value, with a corresponding increase to property, plant and equipment.

3. Significant accounting policies - continued

Asset retirement obligations - continued
The Utility has determined that it has tangible long lived assets with associated future legal obligations for retirement. As the Utility anticipates using the assets for an indefinite period, the date of removal of these assets cannot be reasonably determined, and therefore an asset retirement obligation has not been recorded. When the timing and amount of the retirement can be reasonably estimated, an asset retirement obligation and the corresponding increase in property, plant and equipment asset will be recognized.

Direct financing leases
Investments in direct finance leases are carried at the lower of cost and net realizable value.

Contributions in aid of construction
Certain property, plant and equipment additions are made with the assistance of cash contributions from customers or government. These contributions are deferred upon receipt and are amortized to income on the same basis as the assets to which they relate. Amortization of contributions from customers is netted on the statement of operations against amortization expense.

Deferred licensing costs
Costs related to obtaining water license renewals are deferred and amortized to earnings on a straight line basis over the term of the license. The Utility operates its hydro generation facilities under three separate water licenses, with terms ranging from 17 to 25 years. These costs are treated as intangible assets and are measured at initial cost and amortized over the life of the license.

Employee pension plan
The Utility sponsors an employee defined benefit pension plan which provides benefits based on the length of service and average salaries for the five highest paid consecutive years of service. Employees joining the Utility after January 1, 2002 are not eligible to participate in the defined pension plan. Effective January 1, 2011, the Utility also sponsors an executive defined benefit pension plan and supplemental executive retirement plan. The Utility contributes amounts to the pension plans as recommended by an independent actuary.

The cost of pension benefits is actuarially determined using the projected benefits method, prorated on service, and reflects management's best estimates of investment returns, wage and salary increases, and age at retirement. Pension costs include the adjustments resulting from plan enhancements, actuarial gains and losses, and changes in assumptions which are amortized over the expected average remaining service period of active employees. The excess of the net unrecognized actuarial gains and losses over 10% of the greater of the accrued benefit obligation and the fair value of the plan assets is amortized on a straight line basis over the expected average remaining service period of active employees, which is currently 9 years for the employee plan (2010 9 years) and 5 years for the executive plan. The transitional asset (liability) arising when these policies are first applied is amortized over the average remaining service period of active employees when the amendment is recognized, which is 18 years for the employee plan and 5 years for the executive plan. The expected return on plan assets is based on the fair value of these assets.

Financial instruments
Financial assets and financial liabilities are recognized on the Corporation's balance sheet when the Corporation becomes party to the contractual provisions of the instrument.

Cash
Cash is comprised of cash on hand and in bank accounts less bank indebtedness.

3. Significant accounting policies - continued

Financial instruments - continued

Accounts receivable

Accounts receivable, classified as loans and receivables, are initially measured at fair value. Subsequent to initial recognition, accounts receivable are measured at amortized cost less any impairment.

Accounts payable and accrued liabilities

Accounts payable and accrued liabilities, classified as other financial liabilities, are measured at amortized cost.

Long-term debt

Long-term debt, classified as other financial liabilities, is initially recognized at fair value. Subsequent to initial recognition, long-term debt is measured at amortized cost.

Transaction costs

Transaction costs are presented as a reduction from the carrying value of the related debt and are amortized using the effective interest rate method over the terms of the debts to which they relate. Transaction costs include fees paid to agents, brokers and advisors but exclude debt discounts and direct financing costs.

Derivative financial instruments

Derivative financial instruments are financial contracts that derive their value from changes in an underlying variable. The Corporation has entered into interest rate swaps to manage interest rate risk. The Corporation's interest rate swaps are designated as held for trading and are thus recognized at fair value on the date the contract has been entered into with any subsequent unrealized gains and losses reported in net income during the period in which the fair value movement occurred.

Fair value estimation

The carrying value of the accounts receivable, accounts payable and accrued liabilities approximate their fair value due to the immediate or short-term maturity of these financial instruments. The fair value of the long-term receivable and the long-term debt is estimated by discounting the future cash flows using current rates for financial instruments subject to similar risks and maturities. The fair value of derivative financial instruments is estimated using standard market valuation techniques and is provided to the Corporation by the financial institution that is the counterparty to the transactions.

Environmental liabilities

Environmental liabilities consist of the estimated costs related to the remediation of environmentally contaminated sites. The Utility will accrue a liability and record an expense, related to present or past activities of the Utility, when there is a legal obligation to remediate the contamination and the costs can be reasonably estimated. If the likelihood of the Utility's obligation to incur these costs is either not determinable or the costs cannot be reasonably estimated, the contingency is disclosed in the notes to the financial statements. The Corporation reviews its estimates of future environmental liabilities on an ongoing basis as described in Note 25.

Measurement uncertainty

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The most significant estimates include those for revenue, accounts receivable, property, plant and equipment, asset retirement obligations, employee pension obligations and rate regulated assets and liabilities. Actual results could differ by a significant amount from these estimates. Management's estimates and assumptions, especially those affecting the reported amounts of regulated assets and the Utility's ability to recover the cost of these assets through future rates, are subject to decisions of the YUB as described in note 4.

December 31, 2011 (tabular amounts in thousands of dollars)

4. Financial statement effects of rate regulation

Certain items in these consolidated financial statements are accounted for differently than they would be in the absence of rate regulation.

Where regulatory decisions dictate, the Utility defers certain costs or revenues as assets or liabilities on the balance sheet and records them as expenses or revenues on the statement of operations as it collects or refunds amounts through future customer rates. Any adjustments to these deferred amounts are recognized in income in the period that the YUB renders a subsequent decision. Regulatory assets represent future revenues associated with certain costs, incurred in the current period or in prior periods, which are expected to be recovered from customers in future periods through the rate-setting process. Regulatory liabilities represent future reductions or limitations of increases in revenues associated with amounts that are expected to be refunded to customers as a result of the rate-setting process.

In the absence of rate regulation the Utility's net income would have decreased by $4,923,000 in 2011 (2010 - decreased by $6,893,000). The following describes each of the circumstances in which rate regulation affects the accounting for a transaction or event:

	2011	2010	Expected remaining recovery/ settlement (years)	For 2011 In the absence of Rate Regulation the Utility's Net Income would have increased (decreased) by:
Regulatory assets				
Deferred charges (note 12), net book value				
Feasibility studies and infrastructure planning	$ 14,884	$ 11,463	5 to 10	$ (3,421)
Deferred customer service costs	571	635	10	64
Hearing costs	2,376	1,635	10 to 45	(741)
Dam safety review	95	119	5	24
IFRS planning	566	434	Indeterminate	(132)
Deferred uninsured losses (note 11)	576	432	Indeterminate	(144)
Diesel contingency fund (note 9)	902	891	Indeterminate	(11)
	19,970	15,609		(4,361)
Regulatory liabilities:				
Faro Mine dewatering deferral revenue (note 15)	397	397	Indeterminate	-
Deferred insurance proceeds (note 17)	6,546	6,816	25	(270)
Regulatory provision for future removal and site restoration costs	4,711	4,764	Indeterminate	(53)
Diesel contingency fund (note 9)	902	891	Indeterminate	11
	12,556	12,868		(312)
Net impact of assets and liabilities	$ 7,414	$ 2,741		$ (4,673)
Impact of other items through income statement				
Fuel Price Adjustment				(250)
Total effect				(4,923)

Regulatory assets

(a) Deferred charges

Deferred charges represent costs which have been deferred and are being amortized over various periods. In the absence of rate regulation, GAAP would require such costs to be recognized as expenses in the year incurred.

4. Financial statement effects of rate regulation - continued

Feasibility studies and infrastructure planning
The Utility undertakes certain projects whose objective is to determine the feasibility of a range of solutions. While in progress, the costs of these feasibility projects are included in these accounts. As well, if the feasibility project determines there is not a viable solution, these projects are closed out and amortized to income over a prescribed number of years. These values are also included in the feasibility accounts. The cost of feasibility projects that result in a capital project are transferred to the cost of the resultant project. In the absence of rate regulation, expenses in 2011 would have been $3,421,000 higher (2010 - $5,263,000 higher expenses).

Deferred Customer Service Costs
The costs associated with negotiating terms of service with a new industrial customer. In the absence of rate regulation, expenses in 2011 would have been $64,000 lower (2010 - $65,000 lower expenses).

Hearing costs
These costs are associated with the YUB regulatory proceedings. The costs consist primarily of various rate and project review proceedings. The Utility is directed to defer and amortize the costs over terms at the discretion of the YUB. In the absence of rate regulation, expenses in 2011 would have been $741,000 higher (2010 - $561,000 lower expenses).

Dam safety review
The Utility has a program of conducting reviews of the safety of its dams in accordance with standards set by the Canadian Dam Association. External consultants are hired every five years with intermittent costs incurred in the interim periods. These costs are amortized over five years as approved by the Utility's 1991/92 General Rate Application and reconfirmed in YUB Order 2005-12 and YUB 2009-8. In the absence of rate regulation, expenses in 2011 would have been $24,000 lower (2010 - $119,000 higher expenses).

IFRS planning
These costs are associated with the accounting conversion from Canadian Generally Accepted Accounting Principles to International Financial Reporting Standards. In the absence of rate regulation, expenses in 2011 would have been $132,000 higher (2010 - $179,000 higher expenses).

(b) Diesel contigency fund
The Diesel contingency fund ("DCF") was established by YUB Order 1996-6 through the Negotiated Settlement process. The DCF is administered by the Utility on behalf of the YUB, and as such is recorded as an asset and a liability. The DCF attracts interest based upon short-term bond rates in which the Utility invests the funds. Any negative balance attracts interest at the lowest short-term borrowing rate available to the Utility through its line of credit. Pursuant to YUB Order 1996-6, the Utility from time to time is required to transfer amounts to or from the fund it maintains on behalf of ratepayers to reimburse the Utility for costs associated with diesel generation required when there is not sufficient water for hydraulic generation to meet demand. In the absence of regulation, GAAP would have required any interest earned or incurred to be included in the Utility's net income in the year in which they occurred. In the absence of rate regulation, the Utility's income and expenses in 2011 would have been higher by $11,000 from interest earned on the DCF (2010 - $4,000 higher income and expenses).

(c) Deferred uninsured losses
The YUB has approved the use of a deferral account for uninsured damages and injuries as a means of self-insurance. The account is maintained through an annual provision approved by the YUB. In order to eliminate the deficit rate payers owed as a result of uninsured losses, the Utility was directed by YUB Order 2009-8 to record an annual provision of $100,000 in 2010 and each subsequent year.

4. Financial statement effects of rate regulation - continued

(c) Deferred uninsured losses - continued
In the absence of rate regulation, GAAP would require costs to be expensed as incurred and, therefore, expenses in 2011 would have been higher by $144,000 (2010 - $321,000 higher expenses). The period over which the provision will be recovered is dependent on the magnitude of future actual losses incurred and cannot be estimated.

Regulatory liabilities

(d) Faro Mine dewatering deferral revenue
As directed by YUB Order 1998-5, all revenues, less any incremental costs to provide the service, collected from the Faro Mine under Rate Schedule 34 (Faro Mine Firm Shutdown Power) prior to December 31, 2004, were deferred for the benefit of ratepayers pending direction from the YUB. YUB Order 2005-12 confirmed that effective January 1, 2005 the Faro minesite would be charged the General Service - Government rate so there will be no further increases to Faro Mine dewatering deferral revenue account.

The period over which the remaining liability will be recognized as revenue for the benefit of ratepayers is dependent on future YUB Board orders and, therefore, cannot be estimated.

(e) Deferred insurance proceeds
The deferred insurance proceeds relates to a fire at the Whitehorse Rapids Generating Station in 1997 which, pursuant to YUB Order 2000-3, is being amortized to income at the same rate as the replacement assets. In the absence of rate regulation, GAAP would have required the gain to have been completely recognized as income in the year received. As a result, the Utility's net income in 2011 would have been lower by the amount of the amortization of $270,000 (2010 - $270,000 lower).

(f) Regulatory provision for future removal and site restoration costs
Pursuant to amortization rates approved by the YUB in the Utility's previous general rate applications the Utility has maintained a reserve for future removal and site restoration costs. As a result of the YUB Order 2005-12, effective January 1, 2005, the Utility is required to maintain this reserve as a regulatory provision in addition to any asset retirement obligations. The provision is not to exceed the cumulative value of the provision at December 31, 2004 of $5,757,000. YUB Order 2005-12 also directs the Utility to notify interveners and interested parties when the balance of the provision reaches $2,000,000.

Costs of dismantling capital assets, including site remediation, will be applied to this regulatory liability if they do not otherwise relate to an asset retirement obligation. In a non-regulated industry, future removal and site restoration costs would be limited to asset retirement obligations, and the removal and site restoration costs would be expensed in the year incurred if they did not relate to an asset retirement obligation. In the absence of rate regulation, the Utility's 2011 expenses would have been higher by the amount of actual removal and site restoration costs incurred in the year of $53,000 (2010 expenses - $244,000 higher). The period over which the provision will be settled is dependent on the future costs of demolishing, dismantling, tearing down, or otherwise disposing of the asset, and site restoration net of actual recoveries, and is, therefore, indeterminate.

(g) Fuel price adjustment
OIC 1998/90 directs the YUB to permit the Utility to adjust electricity rates to reflect fluctuations in the price of diesel fuel. The amount by which actual fuel prices vary from the YUB approved rates is deferred and recovered from or refunded to customers in a future period.

In the absence of rate regulation, GAAP would require that actual diesel fuel expenses be included in the operating results of the year that they are incurred. In 2011, fuel expenses were recovered and consequently higher by $250,000 (2010 fuel expense lower by $111,000).

December 31, 2011 (tabular amounts in thousands of dollars)

4. Financial statement effects of rate regulation - continued

Other items affected by rate regulation

The Utility is required under the *Public Utilities Act* to obtain prior approval from the YUB before making changes to depreciation, amortization, and depletion rates and methods. The YUB also permits an allowance for funds used during construction ("AFUDC"). For the year 2010 AFUDC was based on the Utility's weighted average cost of capital. AFUDC is also included in the cost of property, plant and equipment for financial reporting purposes, and is amortized over future periods as part of the total cost of the related asset, based on the expectation that amortization expense, including the AFUDC component, will be approved for inclusion in future customer rates. Because the AFUDC rate for 2010 included a cost of equity component, the amount capitalized in that year exceeds what would otherwise be allowed in the absence of rate regulation. In the absence of rate regulation, revenue for 2010 would be $112,000 lower. The impact on revenue for 2011 is nil.

It is the Utility's policy to charge to income, in the year of disposal, any gain or loss upon retirement or disposal of land or vehicles. As approved by the YUB, the gain or loss on all other property, plant and equipment is deferred and amortized over the expected life of the remaining pool of similar assets. In the absence of rate regulation, GAAP would require the gain or loss on the disposal or retirement of all property, plant and equipment to be included in income in the period of disposal or retirement. The Utility's policy of maintaining a constant capital structure of 60% debt and 40% equity is reviewed by the YUB as part of the rate setting process and in the determination of the return on rate base. In the absence of rate regulation, the Utility would determine the appropriate capital structure solely based on decisions by the Board of Directors of the Utility, which may differ from the current policy.

All amounts maintained as regulatory assets and liabilities are expected to be recovered or settled over the periods noted above. However, there are risks and uncertainties associated with the recovery or settlement related to potential future decisions of the regulator which could result in material adjustments to these assets and liabilities.

5. Cash

The cash balance includes an amount of $7,235,404 (2010 - $2,691,308) that is restricted for the payment of a contractor holdback.

6. Accounts receivable

	2011	2010
Green Infrastructure funding	$ 19,724	$ 22,757
Wholesale energy sales	2,615	3,015
Retail energy sales	1,528	2,940
Other	1,980	1,139
	$ 25,847	$ 29,851

December 31, 2011 (tabular amounts in thousands of dollars)

7. Customer contribution financing

Under the terms of a Power Purchase Agreement with an industrial customer, the Utility agreed to finance the cost of transmission assets built to serve the customer. The Corporation also loaned the Utility cash in an amount equal to this receivable at substantially the same terms which was recorded as long term debt by the Utility. During 2011, this financing was paid in full by the industrial customer, and on the same day, the loan owing by the Utility to the Corporation was paid in full.

8. Direct financing leases

The Corporation's investments in direct financing leases are summarized as follows:

		2011		2010
Direct financing leases	$	162	$	575
Less: current portion		-		413
	$	**162**	$	162

In 1990, the Corporation acquired the building known as Old Yukon College from the Yukon Government for a nominal fee. The building was renovated and is being leased back to the Government for a period of 20 years. At the end of the lease term (in 2011) the Government may purchase the building from the Corporation for a nominal fee. Interest from the lease is recognized as finance income. The investment balance was $Nil in 2011 (2010 - $366,428). The monthly lease payments on the building were $65,348.

In 2003, the Corporation financed an electric boiler system for the Yukon Hospital Corporation for a total cost of $595,898. The repayment terms on this lease stipulate that one half of the energy cost savings resulting from the boiler usage during the year will be repaid against the investment. Interest on this investment is earned at the rate of 7.5% per annum and is recognized as finance income. The investment balance was $162,090 in 2011 (2010 - $208,216).

9. Diesel contingency fund

		2011		2010
Balance, beginning of year	$	891	$	887
Interest		11		4
Balance, end of year	**$**	**902**	$	891

The annual return on investments for 2011 was 1.21% (2010 - 0.50%). The fair market value of these investments is equal to their carrying amount due to the short term maturity of the investments.

December 31, 2011 (tabular amounts in thousands of dollars)

10. Property, plant and equipment

	Cost	Accumulated Amortization	**2011** Net Book Value	2010 Net Book Value
Generation	$ 275,985	$ 60,374	$ 215,611	$ 91,260
Transmission	128,922	18,346	110,576	63,476
Buildings and other equipment	19,949	8,681	11,268	11,376
Distribution	28,265	9,599	18,666	19,119
Construction-in-progress	8,056	-	8,056	91,851
Transportation	4,578	1,624	2,954	2,935
Financial information system	1,303	1,303	-	-
Land and land rights	1,112	-	1,112	1,117
	$ 468,170	**$ 99,927**	**$ 368,243**	$ 281,134

11. Deferred uninsured losses

	2011	2010
Balance, beginning of year	$ 432	$ 111
Provision	(100)	(100)
Losses incurred		
Asset replacement	244	421
Balance, end of year	**$ 576**	$ 432

YUB Order 2009-8 directed the Utility to charge $100,000 to this provision starting in 2010.

12. Deferred charges and intangible assets

	Cost	Accumulated Amortization	**2011** Net Book Value	2010 Net Book Value
Intangible assets:				
Deferred water licensing costs	$ 10,796	$ 5,049	$ 5,747	$ 4,677
Deferred charges:				
Feasibility studies and infrastructure planning	18,522	3,161	15,361	11,463
IFRS planning	566	-	566	434
Hearing costs	5,157	2,257	2,900	1,635
Deferred customer service costs	769	198	571	635
Dam safety review	332	237	95	119
Deferred financing costs	110	77	33	44
	$ 36,252	**$ 10,979**	**$ 25,273**	$ 19,007

December 31, 2011 (tabular amounts in thousands of dollars)

13. Bank indebtedness

The Corporation has access to a $27.5 million line of credit. The account accrues interest on withdrawals at prime less .25%. At December 31, 2011, the balance of this line of credit was $4,782,352 (2010 - $0).

14. Accounts payable and accrued liabilities

	2011	2010
Trade payables	$ 27,239	$ 16,869
Employee compensation	219	428
Other	14	38
	$ 27,472	$ 17,335

15. Faro Mine dewatering deferral revenue

	2011	2010
Faro Mine dewatering deferral revenue account		
Opening balance	$ 397	$ 397
Closing balance	**$ 397**	$ 397

December 31, 2011 (tabular amounts in thousands of dollars)

16. Long-term debt

The Corporation's long-term debt is summarized as follows:

	2011	2010
Bond The Corporation issued a bond at a fixed interest rate of 5.0% per annum. Interest is payable semi-annually. Principal payment is due when the bond expires on June 29, 2040.	$ 98,197	$ 98,169
The Toronto Dominion Bank The Corporation entered into an interest rate swap to convert the interest rate on the Bankers' Acceptances amounts from a variable interest rate based on the Bankers' Acceptances rates to a fixed rate of 2.92% per annum. Principal drawdowns are monthly with the balance due on December 27, 2017.	11,171	12,849
The Toronto Dominion Bank The Corporation entered into an interest rate swaps to convert the interest rate on the Bankers' Acceptances amounts from a variable interest rate based on the Bankers' Acceptances rates to a fixed rate of 4.82% per annum. Principal drawdowns are quarterly with the balance due on March 30, 2017.	5,535	6,481
TD Canada Trust $12,400,000 term note bearing interest at 4.02% (2010 - 7.81%) payable in monthly installments of $94,406 (2010 - $102,000) interest and principal, with the balance due September 30, 2016. The note is guaranteed by the Yukon Government. The terms of the note were renewed October 3, 2011	4,891	5,724
Tr'ondek Hwech'in First Nation liability Long-term liability payable to the First Nation related to the construction of the Carmacks Stewart Transmission Line. This loan is repayable in equal annual principal repayments of $125,000 with the final payment due in 2049. The interest rate at 7.096% is a blended rate based on the cost of debt and the actual rate of return earned by the Utility.	4,750	4,875
Great West Life $5,750,000 mortgage bearing interest at 11.5%, repayable in monthly installments of $60,269 interest and principal with final payment due July 2011. The mortgage is secured by land and buildings.	-	681
Carmacks Stewart First Nation liability Long-term liability payable to several First Nations related to the construction of the Carmacks Stewart Transmission Line. These are non interest bearing, repayable in varying instalments, due in 2028.	371	301
Total	**$ 124,915**	$ 129,080

December 31, 2011 (tabular amounts in thousands of dollars)

16. Long-term debt - continued

The Corporation's long-term debt is summarized as follows:

	2011	2010
Total - balance forward	**$ 124,915**	$ 129,080
Less current portion	3,826	4,270
	$ 121,089	$ 124,810

Long-term debt repayment
Scheduled repayments for all long-term debt are as follows:

2012	$ 3,826
2013	3,955
2014	4,081
2015	4,217
2016	4,071
Thereafter	104,765
	$ 124,915

Fair value
Fair value at December 31, 2011 of $151 million (2010 - $133 million) for all long-term debt including current portions was estimated using discounted cash flows based on an estimate of the Corporation's current borrowing rate for similar borrowing arrangements.

Bond
The Corporation issued a bond in 2010 for the face value of $100 million. The interest rate is 5% and the bond matures June 29, 2040. There are no principal payments due until the bond matures and interest is payable semi annually. The bond was issued at a discount of $0.7 million which will be amortized over the period of the related debt using the effective interest rate. Transaction costs were $1.2 million and includes fees paid to agents and advisors and are presented as a reduction from the carrying value of the related debt and are amortized over the period of the related debt using the effective interest rate.

17. Contributions in aid of construction

	Cost	Accumulated Amortization	2011 Net Book Value	2010 Net Book Value
Contributions from customers since 1998	$ 23,201	$ 4,125	$ 19,076	$ 19,904
Pre - 1998 contributions	1,739	1,118	621	664
Government of Yukon contributions	17,539	1,699	15,840	15,646
Government of Canada contributions	67,277	148	67,129	32,747
Deferred insurance proceeds	11,122	4,893	6,229	6,486
	$ 120,878	**$ 11,983**	**$ 108,895**	$ 75,447

December 31, 2011 (tabular amounts in thousands of dollars)

17. Contributions in aid of construction - continued

The sources of contributions received prior to 1998 were not recorded separately.

The Utility has entered into a contribution agreement with the Government of Canada for Green Infrastructure Funding for the Carmacks to Stewart Transmission Line and the Mayo B Hydro Enhancement projects. The Utility is entitled to reimbursement of 50% of eligible costs to a maximum of $71 million during the period May 2009 to March 2012 subject to meeting structured reporting requirements.

18. Sales of power

	2011	2010
Wholesale	$ 24,170	$ 23,301
Industrial	4,599	3,311
General service	3,342	3,315
Residential	1,535	1,277
Secondary sales	46	644
Other	90	83
	$ 33,782	$ 31,931

19. Operations and maintenance expenses

	2011	2010
Wages and benefits	$ 4,005	$ 3,923
Maintenance		
- hydro, diesel and wind	1,297	1,031
- building and vehicle	1,205	1,011
- lines and substations	898	587
Fuel	2,727	1,189
Water level measurement	156	158
	$ 10,288	$ 7,899

December 31, 2011 (tabular amounts in thousands of dollars)

20. Administration expenses

		2011		2010
Wages and benefits	$	4,735	$	4,204
General office		1,367		1,155
Insurance and taxes		1,083		1,090
Information systems		583		733
Training, recruitment and development		474		570
Environmental		325		298
Board of Directors		314		256
Regulatory loss		248		58
Material management and contracting		26		81
	$	**9,155**	$	8,445

21. Related party transactions

The Corporation is related in terms of common ownership to all Government of Yukon (YG) departments, agencies and Crown Corporations. Transactions with these entities are entered into in the normal course of operations. All transactions with the Utility are recorded at rates set out by the YUB.

The following table summarizes the related party transactions for the year:

		2011		2010
Contributions from YG for Interim Electrical Rebate program	$	3,044	$	3,029
Contributions from YG for Bond interest expense		1,313		-
Account receivable YG		750		152
Capital contributions from YG for Aishihik Hydro third turbine		500		917
Account payable YG		20		-
Program contributions from YG for fish hatchery operations		-		109

22. Pension costs and obligations

An actuarial valuation for funding purposes of the employee defined benefit plan was performed as of January 1, 2010. The next valuation for funding purposes will be conducted as of January 1, 2012. An actuarial valuation for funding purposes of the executive employee defined benefit plan and supplemental executive retirement plan was performed as of January 1, 2011. The pension costs and obligations were based on the data used in these funding valuations and have been projected to December 31, 2011 in accordance with generally accepted actuarial standards.

The fair value of the plan assets is based on market values as reported by the plans' custodians as at December 31, 2011. The plan assets are invested in a pooled balanced fund. The distribution of assets by major asset class is as follows: equities - 45.9% (2010 - 53.1%), fixed income securities - 43.5% (2010 - 37.9%); and real estate - 10.6% (2010 - 9.0%).

December 31, 2011 (tabular amounts in thousands of dollars)

22. Pension costs and obligations - continued

Information about the Utility's defined benefit plan as at December 31, in aggregate, is as follows:

	2011	2010
Accrued benefit obligation determined by actuarial valuation	$ 13,568	$ 11,100
Fair value of plan assets	9,665	8,902
Funded status - plan deficit	$ 3,903	$ 2,198
Unrecognized amounts:		
- Transitional asset (liability)	(192)	119
- Net accumulated actuarial losses	(2,573)	(1,143)
Accrued benefit liability	$ 1,137	$ 1,174
Current portion of accrued benefit liability	-	139
Long-term portion of accrued benefit liability	1,137	1,035
Accrued benefit liability	1,137	1,174
Pension costs	$ 561	$ 510
Employer contributions	$ 596	$ 508
Employee contributions	$ 111	$ 121
Benefits paid	$ 137	$ 132
Significant assumptions for employee defined benefit plan:		
Discount rate - accrued benefit obligation	5.25%	5.75%
Discount rate - pension costs	5.75%	6.25%
Expected long-term rate of return on plan assets	6.50%	6.50%
Assumed rate of salary escalation	3.00%	3.00%
Significant assumptions for executive pension plans:		
Discount rate - accrued benefit obligation	4.50%	-
Discount rate - pension costs	5.75%	-
Expected long term rate of return on plan assets	5.50%	-
Assumed rate of salary escalation	3.50%	-

The accrued benefit liability has been recorded by the Utility and its current portion of $0 (2010 - $139,000) is included in accounts payable and accrued liabilities on the balance sheet.
Employees joining after January 1, 2002 are not eligible to participate in the defined benefit plan.

The Utility makes contributions to a Registered Retirement Savings Plan ("RRSP") on behalf of these employees and to employees hired before January 1, 2002 who belonged to the defined benefit plan and elected to opt out of that plan. The RRSP is a defined contribution plan. The costs recognized for the period are equal to the Utility's contribution to the plan. During 2011 these were $306,000 (2010 - $289,000).

Total cash payments for employee future benefits for 2011, consisting of cash contributed by the Utility to its funded defined benefit pension plan and cash contributed directly to the RRSP were $902,000 (2010 - $681,000).

23. Commitments

Aishihik water license
The Yukon Territory Water Board issued a water use license in 2002, valid until December 31, 2019, for the Utility's Aishihik Lake facility. In addition to maintaining a minimum and maximum water level, this license commits the Utility to meet a number of future requirements including:

- annual payments of $25,000 until 2011 for the purpose of construction and maintenance of a heritage camp and delivery of programs at the camp;
- Heritage Mitigation Plan. The Utility did not incur expenditures in 2011 on heritage projects and the amount to be expended in the future has not yet been determined; and
- annual fish monitoring programs.

Fish monitoring programs are also required under an authorization provided by the Federal Government Department of Fisheries and Oceans, which is valid until December 31, 2019. The costs of meeting these requirements are accounted for as water license costs in the year they are paid.

Contractual obligations
The Utility has entered into contracts to purchase products or services for which the liability has not been incurred as at December 31 2011 as the product or service had not been provided. The commitment at year end is $4,356,000 (2010 - $89,963,000).

24. Contingencies

Carmacks to Stewart Crossing Transmission Project
The Utility completed the construction of the Carmacks to Stewart Crossing Transmission Line project during 2011. In April 2011, the line construction contractor notified the Utility of a potential claim under the contract alleging increased costs of $1,800,000 due to scheduling delays and change in scope caused by the Utility. The outcome of the potential claim is not determinable at this time and no amount has been recognized in the financial statements.

25. Risk management and financial instruments

At December 31, 2011, the Corporation's and Utility's financial instruments included cash, accounts receivable, short-term and long-term receivable, bank indebtedness, accounts payable and accrued liabilities, long and short-term debt and interest rate swaps.

The Corporation has exposure to the following financial risks: interest rate risk, credit risk and liquidity risk. The Corporations' exposure to these risks arises primarily in relation to its long-term debt, but also in relation to its other financial assets and liabilities.

The following presents information about the Corporation's exposure to each of the above risks, and how the Corporation manages those risks.

25. Risk management and financial instruments - continued

Interest rate risk

Interest rate risk is the risk that future cash flows or the fair value of a financial instrument will fluctuate due to changes in market interest rates. The Corporation has debt for which variable and fixed interest rates apply. The Corporation has entered into interest rate swap agreements to mitigate its cash flow exposure to changes in interest rates on its variable rate debt. The Corporation is exposed to fair value risk due to changes in interest rates on its fixed rate debt, including the variable rate debt which has been converted from variable to fixed through the use of interest rate swap agreements.

As at December 31, 2011, the Corporation had two interest rate swap agreements in place with notional principal amounts of $16 million and $8 million. The agreements effectively change the Corporation's interest rate exposure on these notional amounts from floating rates to fixed rates of 2.92% and 4.82% respectively.

The fair value of the interest rate swap agreements at December 31, 2011 was a liability of $824,000. (2010 - $435,000). The interest rate swap agreements cover the notional debt amounts until 2017 at the fixed interest rates noted above. Fair values for interest rate swaps are provided by the financial institution with whom the swaps are held. A 100 basis point decrease/increase in the interest rate assumption would have resulted in an increase/decrease in the interest swap agreements fair value of $449,480 and $439,387 respectively at December 31, 2011 (2010 - $595,876 and $566,215 respectively). During the year the Corporation paid $6.267 million of interest. (2010 - $4.18 million)

Credit risk

Credit risk is the risk of failure of a debtor or counterparty to honour its contractual obligations resulting in financial loss to the Corporation. Financial assets, which potentially subject the Corporation to concentrations of credit risk consist principally of cash, accounts receivable and long-term receivable. The maximum credit risk at December 31, 2011 is the fair value of these assets which totals $34.432 million (2010 - $80.581 million).

The credit risk related to cash is minimized as these assets are held with a Canadian chartered bank.

Accounts receivable are considered for impairment when they are past due or when objective evidence is received that a customer will default. Management has assessed that the credit risk for accounts receivable is minimal since its primary customer which makes up 10.3% (2010 - 10.1%) of the accounts receivable at December 31, 2011, is a regulated utility which has had a history of positive cash flow and no impairment and 76.3% (2010 - 76.2%) of accounts receivable balance is due from the Government of Canada. Consistent with prior years there were no balances owing that are older than 90 days and thus the Corporation did not recognize an allowance for doubtful accounts. There is no history of impairment.

In order to minimize the credit risk on the long-term receivable, management obtained the security of assets for the loan and reviews the recoverable amount at each balance sheet date to ensure that adequate impairment losses are made for unrecoverable amounts. Management has considered the customer's credit worthiness by analysis of the entity's financial statements as at December 31, 2011. Based on this analysis, management expected to collect the amount of the loan in its entirety.

Liquidity risk

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they fall due. The Corporation's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Corporation's reputation through active management of the assets and liabilities and cash flows. The carrying amount of accounts payable and accrued liabilities, and long term debt represents the maximum exposure to liquidity risk. At December 31, 2011, the Corporation's accounts payable and accrued liabilities had a carrying value of $27.4 million (2010 - $17.3 million).

December 31, 2011 (tabular amounts in thousands of dollars)

25. Risk management and financial instruments - continued

Liquidity risk - continued

At December 31, 2011, the Corporation's long term debt had a carrying value of $124.92 million (2010 - $129.08 million) and nil is due in 2011 (2010 - $0.681 million), $4.891 million is due in 2016 (2010 - $5.724 million), $16.706 million is due in 2017 (2010 - $19.330 million), $0.371 million due in 2028 (2010 - $0.301 million), $98.197 million due in 2040 (2010 - $98.169 million) and $4.750 million is due in 2049 (2010 - $4.875 million).

The Corporation had $22.7 million (2010 - $17.5 million) in undrawn credit facilities at its disposal to further reduce liquidity risk.

Fair values
The following table illustrates the fair value hierarchy of the Corporation's financial instruments as at December 31, 2011:

	Quoted prices in active markets (Level 1)	Other observable inputs (Level 2)	Unobservable inputs (Level 3)	Total
Derivative related liability	-	$ 824	-	$ 824

The fair value of the derivative related liability in 2010 was $435,000 and was classified as level 2.

26. Environmental liabilities

The Utility's activities are subject to various federal and territorial laws and regulations governing the protection of the environment or to minimize any adverse impact thereon. The Utility conducts its operations so as to protect public health and the environment and believes its operations are materially in compliance with all applicable laws and regulations.

The Utility has conducted environmental assessments at all its diesel plant sites. At sites where environmental contamination was found and a legal obligation to remediate the site existed, the Utility has conducted a full remediation.

Therefore, as at December 31, 2011 no environmental liabilities, for which a legal obligation exists to remediate, have been identified by the Utility. The Utility will continue to use its Environmental Management System to monitor and assess previous and potential existing environmental liabilities on an ongoing basis.

27. Capital management

The Corporation and the Utility's capital is their equity which is comprised of share capital and accumulated funds in the form of retained earnings. The Corporation and the Utility manage their equity by managing revenues, expenses, assets and liabilities to ensure their objectives are effectively achieved while remaining a going concern.

Corporation's Capital Management Policy
The Corporation's policy is to minimize debt from operations to the maximum extent possible with available cash flows without impairing the working capital needs of the Corporation. The Corporation has no set debt to capital target, nor are there any loan agreements which impose any capital requirements on the Corporation.

December 31, 2011 (tabular amounts in thousands of dollars)

27. Capital management - continued

Utility's Capital Management Policy
The Utility monitors its capital on the basis of the ratio of total debt to total capitalization. Debt is calculated as total borrowings which is comprised of long-term debt, including the portion of long-term debt due within one year. Short term debt related to assets under construction at the balance sheet date is excluded from the debt calculation, as the assets are similarily excluded from the determination of rate base until placed into service. Total capitalization is calculated as total debt plus total shareholder's equity as shown on the balance sheet. The Utility maintains a balance in retained earnings as an indicator of the Utility's equity position.

The Utility has a policy which defines its capital structure at a ratio of 60% debt and 40% equity. This policy has been reviewed and accepted by the YUB.

The long-term debt owing by the Utility to the Yukon Development Corporation of $17.424 million that relates to the Transmission Line Construction Financing is not included in this calculation. This long-term debt is linked with the long-term receivable from an industrial customer. The Utility bears no risk in holding this debt so the amount was removed from this calculation. This long-term debt was paid by the customer during the year (Note 7).

The table below summarizes the Utility's total debt to total capitalization position:

(thousands of dollars)	2011	2010
Long-term debt due within one year	$ 4,974	$ 3,864
Long-term debt	120,190	101,449
Total debt	125,164	105,313
Less debt related to the Transmission Line Construction Financing	-	17,424
Total debt to include in the calculation	$ 125,164	$ 87,889
Share capital	$ 39,000	$ 39,000
Contributed surplus	14,600	-
Retained earnings	29,635	26,720
Total equity	83,235	65,720
Total capitalization	$ 208,399	$ 153,609
Total debt to total capitalization	60 %	57 %

There were no changes in the Corporation's or the Utility's approach to capital management during the period.

28. Non-consolidated financial information

The nature and size of operations of the Corporation and its subsidiary, Yukon Energy Corporation differ substantially. Audited financial statements of Yukon Energy Corporation for the year ended December 31, 2011 are also prepared.

29. Subsequent events

a) On April 27, 2012 the Utility filed a General Rate Application with the YUB for test years 2012 and 2013.

b) Aishihik Third Turbine Project. This project was commissioned into service in December 2011. On March 2, 2012, the general contractor filed a claim with the Supreme Court of Yukon for $4,000,000 plus interest and costs alleging the Utility has not paid for work performed. The Utility has informed the contractor of claims for incomplete contract scope, uncorrected deficiencies and other claims. The outcome of the claim is not determinable at this time and no amount has been recognized in the financial statements.

30. Comparative figures

Certain 2010 figures, which are presented for comparative purposes, have been reclassified to conform with the current year's presentation.