(9:30 a.m.)

MR. NOSEWORTHY, CHAIRMAN: Thank you, good morning. Before we get started, counsel, are there any preliminary matters this morning?

MR. KENNEDY: Yes, Chair. I believe that Newfoundland Power is reporting on some undertakings.

MR. NOSEWORTHY, CHAIRMAN: Okay, thank you. Ms. Greene. Good morning, Ms. Greene.

MS. GREENE, Q.C.: Good morning.

MR. ALTEEN: She's Hydro. *(laughter)*

MR. NOSEWORTHY, CHAIRMAN: I have you in my mind this morning that ... I had her in my mind this morning, that Newfoundland Hydro had some undertakings from yesterday. That was my focus. I apologize.

MR. ALTEEN: No penalty, no (inaudible).

MR. NOSEWORTHY, CHAIRMAN: Mr. Alteen.

MR. ALTEEN: Mr. Chairman, two, I think it was two Fridays ago when John Brown, who was a witness for Newfoundland Power, was on the stand, he gave an undertaking to Ms. Greene in relation to references in the Board's 1995 report on rural service. He was relying upon when he scoped the size of the rural deficit. The 1995 report is the response to RFI CA-2, I guess, and I've filed Mr. Brown's response to Ms. Greene's undertaking with the secretary today, and I guess all we really need to do is mark it.

MR. KENNEDY: Yes. U-NP No. 1.

<u>EXHIBIT U-NP NO. 1 ENTERED IN EVIDENCE</u>

MR. ALTEEN: Thank you.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr. Alteen. No other items, counsel?

MR. KENNEDY: No. I believe Hydro is going to be reporting on undertakings potentially on the break, I believe, this morning.

MS. GREENE, Q.C.: Yes, or depending on where we are with cross-examination. Perhaps I'll be at re-direct.

MR. NOSEWORTHY, CHAIRMAN: Okay.

MS. GREENE, Q.C.: I'll do it then.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Ms. Greene. Good morning, Mr. Roberts. How are you?

MR. ROBERTS: Good morning.

MR. NOSEWORTHY, CHAIRMAN: Good morning, Mr. Kennedy.

MR. KENNEDY: Good morning, Chair.

MR. NOSEWORTHY, CHAIRMAN: I wonder could you proceed with your cross-examination of Mr. Roberts, please?

MR. KENNEDY: Thank you, Chair, Commissioners. Good morning, Mr. Roberts.

MR. ROBERTS: Good morning.

MR. KENNEDY: Mr. Roberts, at some point in your testimony, I think yesterday, you, there were some questions concerning the payment of the dividend in 2002.

MR. ROBERTS: Yes.

MR. KENNEDY: And if I was gathering correctly, I think it was your testimony that the actual request, and you can correct me if I'm wrong here, but the actual request made by Government to Hydro for payment of dividends in 2002 was, and I think the number you stated was $104 million.

MR. ROBERTS: I believe it's approximately $104 million.

MR. KENNEDY: Okay. And then Hydro's procedure, if you will, in making that payment of $104 million, is to first deduct from that $104 million the, what's referred to as the dividend and is actually the re-call sales of electricity.

MR. ROBERTS: That's correct. The flow through of the net re-call revenue comes off the 104. Then the balance is determined to be from Hydro.

MR. KENNEDY: So first of all is that step, is that predetermined by Government or is that a decision of Hydro corporate as to how the $104 million first gets netted down to a dividend?

MR. ROBERTS: Government set the total of what their requirement was of 104, I think it's 104.5, and they were advised that of that amount approximately, I think at that point it may have been $26 million, would be coming from the re-call flow through and the balance will be coming from accumulated retained earnings in Hydro.

MR. KENNEDY: Is there, as far as you're aware then, is there some magic to the figure of $104.5 million? It just seems like an odd number. It's ... or is that determined solely by Government then?

MR. ROBERTS: That's determined by Government and they've provided us as to what they require from Hydro in their fiscal year ending March 31st, 2002.

MR. KENNEDY: Okay. And then by convention, I guess, the first thing to get paid is the re-call energy.

MR. ROBERTS: That's correct. The re-call, is 100 percent pay-out of the net re-call revenue, and as I mentioned, that amount will fluctuate depending on what the sales are in

Labrador to our Labrador interconnected customers.

MR. KENNEDY: And I believe some of the testimony was that the re-call revenue net was a little bit higher than was originally anticipated.

MR. ROBERTS: Yes, it was.

MR. KENNEDY: And so then correspondingly the net of that calculation, being the dividend payment from Hydro, dropped slightly.

MR. ROBERTS: That's correct.

MR. KENNEDY: I wonder if we could just have a quick look at **IC-197**, Mr. O'Rielly? Perhaps fortunate for Mr. Roberts, Chair, my laptop decided to be rather uncooperative last night, so sometimes I'm going to be referring to exhibits and it might be the first time I've seen them in a couple of, in a day as well, but having relied on electronic forums entirely. If we could look at page two of two, Mr. Roberts. This was an exhibit that I have referred to when cross-examining a previous witness, Mr. Roberts, and I'm not sure if you were present during that, but it was, I believe, a question I had of Mr. Hall, I think, may have been Ms. McShane, concerning the actual payment of the dividend from Hydro, and as you recall I believe as well I was having some difficulty in reconciling the retained earnings between the financial statements of Hydro and this IC-197.

MR. ROBERTS: That was in relationship to, I think it was this IC-197 and I believe a DBRS report.

MR. KENNEDY: Okay. I don't think that we need to delve into the actual different between the retained earnings figures between the two documents for the purposes of the point that I'd like to just explore with you here this morning, but pursuant to this IC-197, and just focusing on the year 2001, 2002, the estimate figure, the retained earnings figure for 2001 is stated to be $528,984,000, correct?

MR. ROBERTS: That's correct.

MR. KENNEDY: And that then that's split between the retained earnings, sorry, the, less the CF(L)Co. retained earnings of 234 million 582?

MR. ROBERTS: Yes.

MR. KENNEDY: And then adjusted for non-regulated activity, 25 million 035.

MR. ROBERTS: Yes.

MR. KENNEDY: And then you get a net of the Utility only retained earnings of two sixty-nine three sixty-seven.

MR. ROBERTS: Yes.

MR. KENNEDY: Okay. And when it says Utility only retained earnings, am I assuming correctly when I assume that that means the regulated portion of Hydro?

MR. ROBERTS: That is the calculated regulated retained earnings of Hydro including the revenue or the net revenue from IOCC.

MR. KENNEDY: Okay. So there's another small adjustment ...

MR. ROBERTS: There's ...

MR. KENNEDY: ... to make for the IOCC ...

MR. ROBERTS: If you wanted to try to get to a pure regulated retained earnings, what would have to happen is that you'd have to look at the IOCC and remove the profit and adjust also for dividends because it is part of net operating income and 75 percent of that would still be paid to the province as well.

MR. KENNEDY: Okay. And the adjustment for the non-regulated activity of, in the case of 2001, $25,035,000, that's the re-call revenue.

MR. ROBERTS: That's adjusting out the re-call.

MR. KENNEDY: Alright. And then we see that going from 2001 to 2002 the Utility only retained earnings dropped from $269 million to $208 million.

MR. ROBERTS: That's correct.

MR. KENNEDY: And I take it that that's a result of two things, one, first a net off of the actual dividend that's expected to be paid from those retained earnings in 2002 plus any additional extra retained earnings earned during the intervening period up to the end of 2002.

MR. ROBERTS: Yes. It would include the net income for the year, less the dividends paid.

MR. KENNEDY: Okay. And in questioning, I believe it was Mr. Hall, I think it was established that insofar as the, for instance the bond rating agencies would be concerned, that when they look to investing in Hydro, they look to Hydro as an entire corporate body and all of its holdings and all of its subsidiaries.

MR. ROBERTS: That's correct.

MR. KENNEDY: And that for the purposes of that same bonding company, the, where the dividend comes from insofar as Hydro splitting it between regulated and non-regulated portions of the retained earnings, if you will, is irrelevant to a bonding agency or to a lender of the Company.

MR. ROBERTS: I don't know if I'd quite agree with that. I know in the discussions that we had with DBRS and the presentation in, I think, the spring of this year or early summer, they were certainly advised of the components of the dividend and were advised of our dividend policy that requires us to pay out 100 percent of the net re-call revenue and 75 percent of net operating income. They were also advised that the most current information that we had from Government, that there would be a dividend payment requested of us by the Government's year end, March 31st, 2002, that would be in excess of 75 percent of net operating income for that particular year, so they were certainly aware of it, and what they disclosed in their individual report or what they advise potential bond holders, we have no control over.

MR. KENNEDY: Okay. No, fair enough. I guess the question I have is clearly Hydro would, just from a hypothetical perspective, have the ability to pay this requested dividend of $104 million net of the re-call energy dividend or pay-out of $70 million approximately, 68, I think it is now, that they would have, that Hydro would have, at least theoretically, the discretion to be able to pay that dividend, a portion of it out of the retained earnings achieved from the regulated portion of its business and a portion of it achieved from the non-regulated portions of its business?

MR. ROBERTS: At this point the only significant amount there for non-regulated is the re-call revenue and that's just a timing issue. For instance, just if I may use an example, the $25,035,000 that you see there at the end of December 2001 would be paid to the province by March 31st of the next year, because we have the timing differences to when the province requires the payments and when we actually record them.

MR. KENNEDY: Uh hum.

MR. ROBERTS: So that $25 million would be paid to the province by March 31st of 2002. The amount that you see in there for 2002 would be paid by March 31st of 2003, so you have a lag with the province at any point in time.

MR. KENNEDY: Okay. So, but that's as far as the re-call payment?

MR. ROBERTS: But I guess it's not, it's a policy of Hydro's Board of Directors that has set this policy based on direction by Government, that they require 100 percent of the net re-call revenue.

MR. KENNEDY: Uh hum.

MR. ROBERTS: So that is part of the policy, so that's not an option. That's mandatory. So whatever is left over after that's taken off the total requirement by the province, will represent the dividend that will be coming out of the regulated earnings of Newfoundland and Labrador Hydro.

MR. KENNEDY: Okay. And it might be my pure ignorance now of high finance in a large company such as your own. I guess from a layperson's perspective, in paying out this $104 million you've got three potential sources of money. One is the re-call money and it's Hydro's policy, as you just indicated, as determined by the Board of Directors under direction of Government, that that get paid out 100 percent.

MR. ROBERTS: Yes.

MR. KENNEDY: And that's the $25 million that we see in 2001.

MR. ROBERTS: That would be paid, yes.

MR. KENNEDY: Okay. And so then there's a net then of the overall request for payment of $104 million, which brings us down to something in the order of, well that would be $80 million. And so then Hydro has to determine where this $80 million dividend is going to come from, and then there's two, from a layman's perspective, there's two other sources of this, where this $80 million would come from. One would be from the Utility only retained earnings and one would be from the CF(L)Co. retained earnings.

(9:45 a.m.)

MR. ROBERTS: No. The CF(L)Co., the situation with CF(L)Co. is that any dividends received by Hydro from its shareholding in CF(L)Co. are kept in Hydro. They are used to pay the interest costs on the debt associated with CF(L)Co. $1 million is retained each year to be applied against the principal of the debt associated with the acquisition of CF(L)Co. and the balance is to be paid to the province as well, so the only thing that's allowed to be kept in the case of CF(L)Co. is the interest cost which must be paid on the debt plus $1 million to reduce the principal. The balance of the funds received from CF(L)Co. via dividends also flows through to the province in any particular year.

MR. KENNEDY: So in effect then when, if I'm gathering correctly then, you're saying that the retained earnings in CF(L)Co., at least that line that I see there, 234 million 582 for 2001 ...

MR. ROBERTS: That's an accounting recording of the equity associated with CF(L)Co.

MR. KENNEDY: But so is the Utility only retained earnings, isn't it? It's an accounting number?

MR. ROBERTS: Yes, yes.

MR. KENNEDY: There's not actually $269 million sitting in your bank account.

MR. ROBERTS: I wish it was.

MR. KENNEDY: And in actual fact the pay-out of these 60 or $70 million from the regulated retained earnings causes

Hydro to increase its debt.

MR. ROBERTS: Yes.

MR. KENNEDY: So why wouldn't the same apply to the CF(L)Co. retained earnings, the 234 million 582? What am I missing there?

MR. ROBERTS: There is no cash associated with that either. The only way that could be turned into cash would be to liquidate its investment in CF(L)Co.

MR. KENNEDY: Or borrow, wouldn't it?

MR. ROBERTS: CF(L)Co. can't.

MR. KENNEDY: No, but Hydro could.

MR. ROBERTS: Hydro, I guess, could borrow. Whether or not it could borrow on its investment in CF(L)Co., I really don't know, but all I can tell you is what our current policy is, is that all funds received from CF(L)Co. via dividends are accumulated, we deduct the interest cost and we maintain $1 million for principal repayments and the balance is flowed through to the province. I should also point out that this is an accounting item. Of that $234 million, that's following, and I don't want to try to get into technical terms on accounting, but it's referred to as equity accounting, so that if Churchill made $20 million for the year and we own 66 percent of the company, we will literally record as our equity portion. That doesn't necessarily mean that we've got paid that amount, so that build up in retained earnings is the equity portion associated with the CF(L)Co. net of the costs associated with it.

MR. KENNEDY: So if I'm gathering correctly then, Hydro doesn't have the discretion to make a portion of its payment in any one given year to Government out of the CF(L)Co. retained earnings.

MR. ROBERTS: Not in my opinion, we don't.

MR. KENNEDY: And this is based on your understanding of a policy of Hydro itself.

MR. ROBERTS: The policies set by the Board are, as I outlined, that it will pay the flow through of the net dividend income received from Churchill Falls, plus it will pay 75 percent of the net operating income of Hydro plus 100 percent of re-call revenue to the province.

MR. KENNEDY: And we know that Government has in effect countermanded the 75 percent dividend policy on the retained earnings.

MR. ROBERTS: Hydro's Board of Directors approved that policy of 75 percent of net operating income.

MR. KENNEDY: Okay. The other topic I wanted to ask some questions about, Mr. Roberts, refers to the deferral of the rate hearing costs.

MR. ROBERTS: Yes.

MR. KENNEDY: And I think it's Hydro's position, if I'm gathering correctly, that it proposes that those hearing costs be amortized over a period of two years, correct?

MR. ROBERTS: That's correct.

MR. KENNEDY: And that those two years would be 2002 and 2003.

MR. ROBERTS: Yes, it would.

MR. KENNEDY: And that's on the rationale that Hydro intends to be back before this Board in 2003 with another rate application which would potentially impact its rates for 2004.

MR. ROBERTS: That's correct. 2004 would be the test year.

MR. KENNEDY: Okay. And you'll agree with me, will you, that the hearing costs themselves are incremental in nature.

MR. ROBERTS: Yes.

MR. KENNEDY: They're not costs that would otherwise avoided, that could otherwise be avoided.

MR. ROBERTS: That's correct.

MR. KENNEDY: You'll agree with me, won't you, well, I think it's a stated fact, that this is the first application that Hydro has made to the Board for a rate increase since 1992?

MR. ROBERTS: Yes.

MR. KENNEDY: And that, will you agree with me that this has been a fairly thorough review of Hydro's internal financing and operational issues.

MR. ROBERTS: There is no doubt about that.

MR. KENNEDY: And that much of that goes, much of its review and analysis of Hydro's operations and finances dates back to a period, in some instances beginning in 1992?

MR. ROBERTS: We have certainly filed information reflecting '92 to date. There may be other information that's filed going back past 1992.

MR. KENNEDY: Well, for instance, your hydrological records go back 30 years, but ...

MR. ROBERTS: And I also mention, the vein that I was using it was, as an example, yesterday the Consumer Advocate had me back to the 1985 rate hearing when the Rate Stabilization Plan was first introduced, so I fully acknowledge that most of the emphasis has been between '92 and 2002, but there has also been other items been raised from even years prior to 1992.

MR. KENNEDY: For instance, the schedule that we have up in front of us right now, **IC-197**, the request for information and the subsequent reply was for the period 1992 through to the test year of 2002.

MR. ROBERTS: Yes, and that's fairly normal from my experience in the regulatory environment and I have been before this Board starting in 1995 *(sic)* for ... I think this is my fourth or fifth hearing.

MS. GREENE, Q.C.: I think he meant '85.

MR. ROBERTS: 1985. We have always started on the point of when we last appeared before the Board and came forward to the presentation or the hearing that we're involved in now.

MR. KENNEDY: And so you'll agree with me then that many of the issues that we have been dealing with and are likely to deal with until the completion of this hearing relate to operational decisions and issues of Hydro during the period '92, '93, '94 and so on, right up through to today.

MR. ROBERTS: There has been a lot of historical information provided. The question is, is how it will be used in determining 2002 forward. I look at it from the perspective of some of this information, you know, just use one particular aspect that I have direct familiarity with, is that annually Hydro has been subjected to an audit by auditors appointed by the Public Utilities Board, so issues, if they were there, were being raised and provided to the parties of these annual reviews that are conducted on Newfoundland and Labrador Hydro, and I also understand they're done on Newfoundland and Labrador *(sic)* Power, so some of these things have certainly been brought to people's attention, just haven't been sitting here for ten years waiting to be addressed.

MR. KENNEDY: No, no, and I appreciate that and I'm not trying to imply anything other than that, but clearly this information of Hydro that you just alluded to, the review conducted by the Board's financial advisor, the annual review, that that, and that's information that Hydro is being freely forthcoming with and being provided to the Board. Clearly though you recognize that the parties involved in the hearing, for instance, for this application weren't around during that period of time in 1992 to date and therefore this is their first opportunity to do a thorough review of those documents that Hydro has been filing during the intervening period.

MR. ROBERTS: I'll acknowledge that one.

MR. KENNEDY: In Hydro's case we're expected to be back in 2003, would you agree with me that because of the ground that's being covered in this application, that it's reasonable to expect that the 2003 application may not be as broad or general in scope as this one?

MR. ROBERTS: I certainly hope so from a personal perspective that it will be a lot less.

MR. KENNEDY: So would you agree with me then that it would be reasonable to consider that the cost of this hearing, being somewhat of an educational process for the panel and for the parties, are extraordinary in that regard?

MR. ROBERTS: I would suggest that they are certainly higher than a normal rate hearing, if you're back, say, every three or four.

MR. KENNEDY: And that some of the information, for instance, that is being gained in this hearing, both again by the panel and by the intervenors, would be of benefit to the parties in 2003, if in fact Hydro does come forward with an application?

MR. ROBERTS: Provided the parties are still here.

MR. KENNEDY: Yes. And have memories of ...

MR. ROBERTS: Yes.

MR. KENNEDY: ... fond memories of 2001.

MR. ROBERTS: I guess the question being is, are you going to use the information here or will it be asked again.

MR. KENNEDY: Exactly. But presume ...

MR. ROBERTS: For that we don't have any control over and if the information is asked, then we'll gladly try to provide it.

MR. KENNEDY: And so presumably, for instance, the questions that I was just asking you about the retained earnings pay-out by Hydro and whether that's available to be paid from the non-regulated portion of Hydro and your explanation of why in fact that can't be achieved, is not a question hopefully that I would ask again in 2003, if in fact I was here, correct?

MS. GREENE, Q.C.: Can we have an undertaking about that, I wonder? *(laughter)* And can we have an undertaking it will not be different counsel? *(laughter)*

UNIDENTIFIED SPEAKER: That's the undertaking you want (phonetic).

MR. KENNEDY: Yeah. So, Mr. Roberts, I guess the point you can probably surmise that I'm getting at is some of the expenses related to this hearing are both backward looking related, that this application has involved a review of the issues that have transpired over the period of time since 1992, and as well educational in scope will benefit the panel and the intervenors and whatever parties and solicitors are involved in subsequent hearings in those subsequent hearings.

MR. ROBERTS: I agree.

MR. KENNEDY: And so wouldn't you agree with me then that it's reasonable to suggest that the hearing costs themselves for 2001 be amortized over a greater period than the suggested two-year period?

MR. ROBERTS: That's certainly one option. What Hydro looked at was the impact that it would have going towards the future, like I personally don't think there's any doubt we're going to be back in 2003 unless there's really a fortuitous event out there that will result in a significant windfall to Hydro. What we were looking at is if you went three years, if you went five years, you are now going to impact the projected rate base for 2004, so what we were doing in this particular case was trying to narrow the gap to 2002 and 2003 when we do come back in 2003 for 2004. I have no idea at that point how far that particular hearing would carry us out.

MR. KENNEDY: Well now you haven't closed off your books for 2001 yet, have you?

MR. ROBERTS: No.

MR. KENNEDY: So you could book some of the hearing costs in 2001, couldn't you?

MR. ROBERTS: I would certainly hope that from an accounting perspective that we would be able to have enough information to accrue all of these costs in 2001 to the extent that we can. We recognize that these were estimates that we were trying to put forward to the Board for approval to defer and of course it would be on the understanding that these numbers would try to be confirmed to actual as close as we could prior to the Board making its order.

(10:00 a.m.)

MR. KENNEDY: So if I'm gathering correctly though, that there's nothing to prevent in, just leaving aside the issue of using 2004 as one of your amortization years for the deferral of the hearing costs, that there's nothing to prevent Hydro from absorbing some, if not all, of the hearing costs in 2001.

MR. ROBERTS: Hydro could absorb them all. For a deferral basis, we do require approval of the Board in which to do it because under the generally accepted accounting principles there is no basis to defer these costs. The only way we would be able to defer them would be a regulatory order authorizing us to defer these costs and recover these costs in future rates.

MR. KENNEDY: Would you be able to, Mr. Roberts, provide an update of your Schedule 1A as filed on October 31, 2001, with the hearing costs amortized over a four-year period instead of a two-year period and what impact that would have on your revenue requirement?

MR. ROBERTS: We could. I have some qualification now to what I'm saying. If you just wanted us to deal with that and ignore the impact on interest and re-running through all the hoops and ... and that could be done relatively quickly, I believe, if you just want to say here's what it would be, because you're only taking, you're taking that $2 million and you wanted it over four years.

MR. KENNEDY: Yes, but I guess there's an impact there on the interest as well, is it not?

MR. ROBERTS: There'd be an impact on, to the interest, depending what would happen and spinning back through what the rates would be because you have to get sort of cost of service and allocate between Newfoundland Power and the industrial customers, the rates into Labrador. It's not a very simple process in which to do it.

MR. KENNEDY: Okay. So that's a simple request that involves a lot of work.

MR. ROBERTS: Yes, it does.

MR. KENNEDY: That's what you're telling me.

MR. ROBERTS: But if you want to ballpark the amount ...

MR. KENNEDY: Yeah, that's fine.

MR. ROBERTS: If you're looking at it, you're talking $2 million over four years.

MR. KENNEDY: So just split it ...

MR. ROBERTS: So it'd be a half million dollars, so the revenue, the total revenue requirement would be altered by a half million dollars in 2002, and what that would translate down into the rates, depends on the split between the various customers.

MS. GREENE, Q.C.: I wonder if counsel could indicate whether the answer that Mr. Roberts just gave is satisfactory.

MR. KENNEDY: Yes, that's satisfactory. Yes, thank you. Mr. Roberts, on to another topic. I have a lot of topics, none of them particularly long, so ...

MR. ROBERTS: Okay.

MR. KENNEDY: On **page six of your pre-filed testimony**, at line eight, or line six, "What is Hydro's projected long-term debt for 2001, 2002?" And, "Schedule 10 of my evidence provides specific details on Hydro's long-term debt for those two years." And then you go on to provide some information about Hydro's borrowing strategy being one of short-term promissory notes and long-term debentures, and that "Pursuant to Section 33 of *The Hydro Corporation Act* our short-term debt as prescribed by Order-in-Council may not exceed $300 million." And then you go on describe how, well, it's Hydro's practice to borrow from the $300 million and then it allows you some financing flexibility because you can then take out long-term debt when it's perhaps the best time to do it as opposed to being forced to go to the market ...

MR. ROBERTS: That's correct.

MR. KENNEDY: ... to borrow long-term debt.

MR. ROBERTS: Yes.

MR. KENNEDY: And that would be a normal or typical financing mechanism for a corporation, size and complexity of Hydro.

MR. ROBERTS: Any large corporation will be monitoring its mix of short and long-term and trying to use whatever advice it can probably obtain to determine where the market is looking towards the future, in trying to find that optimum time to switch from short-term to long-term and lock in that particular rate.

MR. KENNEDY: Anecdotally did you note that the United States Treasury has stopped issuing ...

MR. ROBERTS: 30-year ...

MR. KENNEDY: ... long-term debt? It's ...

MR. ROBERTS: It stopped ...

MR. KENNEDY: ... no longer issuing a 30-year bond.

MR. ROBERTS: 30-year debt, that's correct.

MR. KENNEDY: And I understand that, and I believe there's been some expert testimony on it, that that's based on the rationale that at his point in time it makes more sense for them to borrow on short-term money as opposed to the long-term bond issues.

MR. ROBERTS: That could be correct. I'm not sure for a reason as to why. I am aware that they did stop issuing 30-year bonds.

MR. KENNEDY: Okay. And were you here when Dr. Kalymon testified? Portions of it, I believe.

MR. ROBERTS: That was for the consumer, yes.

MR. KENNEDY: Yes. And Dr. Kalymon provided some testimony at the beginning of his testimony in which he provided an update to some of the figures that were included in his pre-filed evidence.

MR. ROBERTS: Yes.

MR. KENNEDY: And it was noted by Dr. Kalymon that there's been a dramatic change in the market rates for short and long-term debt, and I believe he used significant or dramatic effect on short-term money and a, certainly a corresponding change in the long-term money since even he filed his report in earlier 2001.

MR. ROBERTS: I believe he did indicate there was a fairly significant drop in short-term rates but I think in the long-term rates it was like 50 to 75 basis points, when he looked at it, which I think was November 9th.

MR. KENNEDY: Right. Can you tell me when the Order-in-Council limiting Hydro to a $300 million cap was instituted?

MR. ROBERTS: No, I can't. It has been there for some time but the actual date, I wouldn't have that information.

MR. KENNEDY: You've been involved with Hydro in the position, as position of Controller for how long?

MR. ROBERTS: I've been in my position since 1985, and the reason why I wouldn't have in-depth familiarity with it is that there is a separate treasury function within Hydro, so there is an actual Treasurer for the organization with the appropriate staff in place who does all this work.

MR. KENNEDY: Okay. So as far as you're aware though, the $300 million cap, that's been present since your involvement as Controller with Hydro?

MR. ROBERTS: I believe it's been there ever since, it may go back to 1985, I'm not sure, but it has been ... it's not a recent addition, if you're referring to the last five years or so, to the best of my knowledge.

MR. KENNEDY: Okay. At page seven and then going on to page eight of your pre-filed testimony, you provide some discussions concerning the calculation of the interest charge associated with the Rate Stabilization Program.

MR. ROBERTS: Yes.

MR. KENNEDY: And as I understand it right now, the current interest charge associated with the Rate Stabilization Account, or Program, is the embedded cost of debt, correct?

MR. ROBERTS: That's correct.

MR. KENNEDY: And pursuant to your Schedule 9, I believe it is, the embedded cost of debt was calculated to be 8.345 percent at the time. I think that might have been revised since then.

MR. ROBERTS: Yes. That was in the initial filing, 8.345.

MR. KENNEDY: And that pursuant to Hydro's application, it's recommending that it move to a weighted average cost of capital for calculating the interest that accumulates on the Rate Stabilization Program balance.

MR. ROBERTS: Yes, with the adaption of the rate base methodology that comes with it.

MR. KENNEDY: And again, pursuant to the original filings under Schedule 8, that weighted average cost of capital works out to 7.399 percent.

MR. ROBERTS: That's correct.

MR. KENNEDY: Now, just so we're clear, the weighted average cost of capital of 7.399 percent as originally filed is lower than your embedded cost of debt because your proposed rate of return on your equity is only at three percent, correct?

MR. ROBERTS: Correct.

MR. KENNEDY: If in two years' time Hydro were to take an application seeking a, what it considers to be a more appropriate rate of return of, say, 11 percent, if, depending on what the market conditions are at the time, the weighted average cost of capital will in fact be higher than your embedded cost of debt potentially, correct?

MR. ROBERTS: It could potentially be there but it could also still be less. It's depending on what the embedded cost ...

MR. KENNEDY: Capital structure is and ...

MR. ROBERTS: Capital structure, what the embedded cost of debt is.

MR. KENNEDY: What your market rates are for ...

MR. ROBERTS: There's all kinds of variables that could impact it.

MR. KENNEDY: There's a host of issues involved, wheels within wheels on that one.

MR. ROBERTS: No doubt that there are other factors that will have an impact as to what it will actually be in two or three years' time.

MR. KENNEDY: Sure. Now, I believe it's the case as well that the, and I believe this is noted in your pre-filed testimony as well, that the assets associated with the rural rate, the rural part of and isolated parts of Hydro's operations, are treated differently for the purposes of calculating a rate of return on those.

MR. ROBERTS: That's correct.

MR. KENNEDY: And that instead of being included in your overall rate base and being titled to a weighted average cost of capital for the rate base, it's actually assessed the weighted average cost of your debt. Is that correct?

MR. ROBERTS: That's correct.

MR. KENNEDY: And you calculate that at Schedule 7 of your pre-filed testimony to be 6.941 percent.

MR. ROBERTS: That's correct.

MR. KENNEDY: And that's probably changed as well as your borrowings fluctuate.

MR. ROBERTS: Yes, I think that's changed slightly since the update for October.

MR. KENNEDY: And could you just explain to us again what the rationale is for why the isolated assets receive a different treatment than the rest of your asset base?

MR. ROBERTS: In at least the '92 hearing and I think the hearing prior to that, the issue of earning an interest margin arose on Hydro rural assets because of the fact that these assets were forming part of the rural deficit, and what the Board decided is that Hydro shouldn't make a profit on assets that were contributing to a deficit, so you shouldn't be inflating the deficit higher by earning a profit on assets that are associated with that deficit.

MR. KENNEDY: Okay. So there was a rationale for why the isolated assets should be treated separately and it was associated with the fact that there was a deficit associated with operating those isolated assets.

MR. ROBERTS: That's correct, and that was addressed in two hearings by the Board.

MR. KENNEDY: Sure, okay. Now the Rate Stabilization Program, been much discussion on that and I don't know if I'm going to over-simplify it, but is it fair to say that one of the principal objectives of the Rate Stabilization Program is to provide both rate stability for the ratepayers and as well revenue stability for Hydro?

MR. ROBERTS: It certainly provides stability to customers and it does contribute to some stability to Hydro.

MR. KENNEDY: It insulates Hydro from being subject to variations in load and errors in forecast, if you will, on its hydrology, for instance, and thermal production.

MR. ROBERTS: I wouldn't go so far as to say errors in hydrology, but it does account for the variances in hydrology for which we have no control over the water and whether or not it's going to rain or it's going to be dry, but it does provide Hydro with some protection relative to the hydrology, fuel price, and in the case of load. It doesn't pick up and adjust for efficiency either in either respect.

MR. KENNEDY: Now, Mr. Fitzgerald asked you some questions, I believe, on hypotheticals about whether if in fact there was a positive balance in the Rate Stabilization Program account, whether there would be an accounting by Hydro of any interest earned, and you indicated, well, it's not exactly interest earned, it would just be less interest paid and that that would be accounted for, less interest paid by Hydro overall by virtue of a positive account in the RSP.

MR. ROBERTS: In the case of the RSP, the RSP is treated as a self-financing asset, so we add interest or we credit interest, depending on the balance in the plan, so the intent is that we are always indifferent so that if we have funds from a customer that we owe them to, we will give them the interest. If they owe us money, we will charge them the interest, and so we are held indifferent from it.

MR. KENNEDY: There was, and you may be able to help me here, there was an exhibit that we looked at, I believe it was yesterday, showing interest calculating, calculated based on your short-term borrowings of 4 1/2 percent. Do you recall looking at an exhibit?

MR. ROBERTS: Yes.

MR. KENNEDY: And I'm wondering whether ... let me put it this way, when was it that the RSP account first started accumulating what you would call a significant deficit?

MR. ROBERTS: I only have in my evidence the balances in the plan from '92 up to 2002 but you're really starting to only see the plan start to increase basically starting in '96 and starting to come forward, and that's when you're starting to hit extremely high prices in fuel and you may also be experiencing some below average water years as well which would impact this plan.

MR. KENNEDY: So according to ... and that's Schedule 14 of your ...

MR. ROBERTS: That's correct.

MR. KENNEDY: ... pre-filed testimony. And according to that Schedule 14, there was in fact a positive balance in the Rate Stabilization Plan in 1994.

MR. ROBERTS: Yes.

MR. KENNEDY: That would be year end 1994, I take it, or ...

MR. ROBERTS: Yes. That would be calendar year end December 31.

MR. KENNEDY: Okay. But by the year end 1995, that positive balance is switched over to a deficit of $12.9 million in total.

MR. ROBERTS: Yes.

MR. KENNEDY: Okay. And then it's been continuing to grow and rather rapidly for the period 1995 through to 1998, and then it backed off a bit and now, according to Hydro's application, you're forecasting that the Rate Stabilization Program is, unless otherwise adjusted, likely to grow again.

MR. ROBERTS: That's correct.

(10:15 a.m.)

MR. KENNEDY: Now, when the Rate Stabilization Account started to climb in that period in 1995 to 1996, and in fact you were, I guess again from a layperson's perspective, booking revenue, if you will, but it being uncollected because you had yet to claw back that portion of the revenue associated with the RSP. Would this have placed pressure on Hydro to increase its borrowings? Does Hydro need to increase its borrowings because of the RSP account climbing, the deficit?

MR. ROBERTS: The borrowings would happen automatically from the point of view that if you buy a shipment of fuel and it's costing you $20 million to buy the shipment of fuel, well, shortly after the fuel is received, within the payment terms and arrange ... the fuel is paid for. As the fuel is consumed and this receivable is created, then we will start setting this amount up and adding interest to that that's removing the other side of the payment of the interest that was associated on the initial purchase, so it's a timing factor of ... you'd have a liability over here and you have a receivable over here and you're incurring interest on both and you're holding yourself equal because it will be paid.

MR. KENNEDY: And because of the way the Rate Stabilization Program operates, it's the case, isn't it, that all else being equal the fuel purchases, for instance, by Hydro and its borrowings in order to achieve those fuel purchases are short-term in nature?

MR. ROBERTS: It initially starts at short-term but I guess Hydro just runs a promissory note balance, and as we discussed earlier, this $300 million amount, and that includes purchase of fuel, it would include capital, it would include paying salaries, whatever. Revenue flows in and costs come out and here's what's happening on that float, and then when you reach an optimum time that you want to convert some of that short-term to long-term, then an amount of that promissory notes are converted but it's not traceable back to specific items.

MR. KENNEDY: But, and it is the case that the overall interest payment by Hydro is the overall interest payment by Hydro. It's going to form the revenue requirement regardless.

MR. ROBERTS: Yes.

MR. KENNEDY: But that whatever interest you associate with the RSP gets booked into the RSP and therefore a portion of the interest goes to the RSP and a portion of it remains in your current account, if you will.

MR. ROBERTS: That's correct.

MR. KENNEDY: And so if we put less interest associated with the RSP, it would decrease the RSP balance in effect but it's still not going to impact Hydro overall because it just means more interest in the current year.

MR. ROBERTS: Well, we have to charge the RSP what the embedded cost of debt is.

MR. KENNEDY: Well, let's not make that presumption just yet, but I'll give you an opportunity to make that presumption in a moment. It is the ... I just want to establish first that if Hydro pays $1 in interest, a portion of that is associated with interest accumulated on the RSP account and then the remaining portion is just the interest that Hydro pays and would form part of its revenue requirement for a given year, it's current year, and I take it that's probably a gross over-simplification of your interest dynamics.

MR. ROBERTS: I'll accept what you're saying and see where it leads me.

MR. KENNEDY: Okay. And so if we associated a lower interest with the deficit accumulated in the Rate Stabilization Program, it would help provide some, it would help alleviate, if you will, the amount of the deficit in the Rate Stabilization Program, would it not, because you'd be booking less interest into the RSP account itself?

MR. ROBERTS: Yes, but we still have to pay the interest costs on the other side.

MR. KENNEDY: Absolutely. And so you would still have to pay the interest and it would still form part of Hydro's revenue requirement.

MR. ROBERTS: Yes.

MR. KENNEDY: Okay.

MR. ROBERTS: But at the end of the day it's still going to be paid, either through an RSP adjustment or through a change in your base rate and the mill rate.

MR. KENNEDY: Right. But if you were to associate a lower interest with the RSP account, your RSP account deficit would not be as high as you're stating it to be as of a given moment in time. For instance, your 2001 forecast, which I appreciate was well prior to many of these dramatic events in the fall that had an impact on the price of oil and the Canadian dollar and your hydrology is changed and so on and so on, but at the point you were filing this your forecast for 2001 was an RSP account deficit of $87.4 million.

MR. ROBERTS: That's correct.

MR. KENNEDY: And a portion of that $87.4 million would be the interest accumulated that Hydro has associated to that Rate Stabilization Account, the principal amount.

MR. ROBERTS: Yes, but the biggest impact on that plan is not interest, it's the components of water and fuel.

MR. KENNEDY: I appreciate that and it's probably orders of magnitude in light of the fact that the interest is, well, either six percent or seven percent or eight percent.

MR. ROBERTS: Yes.

MR. KENNEDY: But nonetheless if we're attempting to live within an existing cap of $50 million and trying to avoid increasing that cap, this would be one mechanism, would it not, to, from an accounting perspective, to keep the deficit in the Rate Stabilization Program below that cap, whatever it may be. It would provide some relief to the Rate Stabilization Program by associating a lower interest payment.

MR. ROBERTS: It will reduce that balance that's owing, but it increases the rates on the other side, so ...

MR. KENNEDY: I understand that.

MR. ROBERTS: ... I'm not so sure that you really gain anything except for complexity, and in today's environment of being regulated on a return on rate base, it becomes, I think, a little bit more complex now where you are in a situation where both the Rate Stabilization Plan is financed with debt and equity, so ...

MR. KENNEDY: Well, let's just go there for a second. The Rate Stabilization Program had its deficits start to accumulate in 1996 really, and that prior to 1995 there was no deficit in the RSP program, correct?

MR. ROBERTS: If you go back into history to '86 and come forward, there have been reversals in both directions.

MR. KENNEDY: Okay.

MR. ROBERTS: So from the point of view of staying in a position where money is owing to Hydro, you're starting to see it in '95. '96 was growing, '97 was, growing some more in '98, '99 is gone down, 2000 is basically flat in comparison to '99, and 2001 is expected to increase.

MR. KENNEDY: And just so I'm clear, Hydro's financing, and I appreciate that it's a float or a drawdown on your promissory note, is not associated with a specific asset, but that the deficit being accumulated in the Rate Stabilization Program needs to be financed by Hydro through debt.

MR. ROBERTS: It could be short (inaudible) as well as long. That's why the embedded cost of debt was used.

MR. KENNEDY: And you use ... and you initially use short-term borrowings to accomplish that objective and it's when your short-term borrowings get to a certain point in the overall $300 million cap that the Government has set that Hydro would time to go to the market in seeking long money.

MR. ROBERTS: Yes, and I guess I can only go back and say is that some of this balance in the plan is, depending on your point in time of when you pick, some of it already in short, some of it's already in long at that point, so there's really no mechanism in which to say how much of that plan is in short versus long, because it's just ...

MR. KENNEDY: Well we ...

MR. ROBERTS: ... a float of piece of debt ...

MR. KENNEDY: We do know that of the money that's there now, the borrowings to finance it would have all taken place post 1995, correct?

MR. ROBERTS: No. Hydro's done borrowing since 1995.

MR. KENNEDY: But, yes, since 1995.

MR. ROBERTS: We've done two in 2001 as an example.

MR. KENNEDY: Yes. I'll leave that. Mr. Roberts, there was reference to an incentive program for Hydro's executives being introduced on a pilot basis.

MR. ROBERTS: Yes.

MR. KENNEDY: Are you a participant in that?

MR. ROBERTS: Yes.

MR. KENNEDY: Is it your department that keeps track of the operation of that pilot incentive program?

MR. ROBERTS: That would fall underneath the responsibility of Human Resources. They administer all pay plans for the organization.

MR. KENNEDY: Can you give us some idea of the flavour of that incentive program insofar as it applies to you in your position in carrying out your duties as Controller? What's your incentive? How is it measured, the efficiencies, if you will?

MR. ROBERTS: I'm just trying to go from memory now. It's not something that I have in the back of my mind. I have departmental objectives as well as participation in divisional objectives and corporate objectives, so targets have been established for those objectives and the remuneration that could possibly be obtained is determinable on whether or not there is a movement from that objective.

MR. KENNEDY: In the department objectives, can you give us some idea of what kinds of objectives that you would be aiming for as part of that department?

MR. ROBERTS: Objectives can vary by the department, but, for instance, one of the ones that I would have as an objective is the continuation of training to area offices' staff related to our new JD Edwards system, so I would make a commitment that I want to have "X" number of visits to those particular areas to train staff in those areas, so that, you know, would be a type of an objective that will be set on me and I attain that and I can exceed it or whatever the case may be, then the remuneration will be accordingly.

MR. KENNEDY: Would there be or are there any objectives related to the financial operation of Hydro that you'd participate in? In other words ...

MR. ROBERTS: I share in the corporate.

MR. KENNEDY: That's the overall corporate objective.

MR. ROBERTS: Yes, because I contribute to that.

MR. KENNEDY: At the department level though, do you have any ...

MR. ROBERTS: At the department level, the objective is based on my budget as to whether or not I can achieve my budget, can I do better than my budget. That's the objective that would be in my particular case related to my share of that budget, but I also share in the responsibility related to the corporate as well.

MR. KENNEDY: Sure, okay. So just to make clear, there are financial objectives which you have the ability to ...

MR. ROBERTS: I have the ability to control ...

MR. KENNEDY: ... play a role in achieving.

MR. ROBERTS: ... control and to participate ...

MR. KENNEDY: A direct role.

MR. ROBERTS: Yes.

MR. KENNEDY: Okay.

MR. ROBERTS: I have both.

MR. KENNEDY: Yes, so directly to your own department and indirectly to ...

MR. ROBERTS: Indirectly ...

MR. KENNEDY: ... the overall corporate objectives.

MR. ROBERTS: ... contribute to the corporation as a whole.

(10:30 a.m.)

MR. KENNEDY: I understand that Hydro has implemented some, an FTE Program in 2001. Are you aware of that?

MR. ROBERTS: It hasn't quite implemented an FTE System. At this point all that has been calculated is a full-time equivalent based on the actual results for a particular month. We do not have a system in place yet, to enable to do our budget and our forecast on that basis. We only have part of the requirement for it. And if I may, for a permanent employee such as myself, it's relatively easy to determine a full-time equivalent. The difficulty comes up, it's in the budgeting for hourly wages and how many hours are within those dollars and trying to get that information recorded some place so that you can report and track. The actuals are relatively easy to obtain because it is history and it's a routine that's written against your payroll system saying here are the results, how many FTEs come out of it.

MR. KENNEDY: So would the tracking of the FTEs going forward be a responsibility of you as Controller?

MR. ROBERTS: Responsibility, I will have responsibility for my area. Reporting would be provided by Human Resources by division and I would have the responsibility to account for my particular area on forward through to the Vice-President of Finance because of the functions of the various divisions.

MR. KENNEDY: Okay. So, but it wouldn't fall to you as Controller of the Company to be tracking FTEs for the entire Hydro Corporation.

MR. ROBERTS: I may be involved in having the system developed ...

MR. KENNEDY: Okay.

MR. ROBERTS: ... but the actual responsibility for control of that, my responsibility may be to be having the system in place. I may even end up generating the reports yet but that's yet to be resolved, but the actual accounting for that would fall back to the responsibility of the individual business unit managers in each division.

MR. KENNEDY: So does the JD Edwards system allow for the tracking of the FTEs or is this another effort that Hydro has to make in order to ...

MR. ROBERTS: I really can't answer that one yet. There are a lot of things that are in JD Edwards that, from my perspective, we can utilize and we are endeavouring to utilize as much as we can as quickly as we can do the investigation and see if it's doing what we require.

MR. KENNEDY: Okay. In **Grant Thornton's Report, I believe it's their 2001 report**, and take it out because I will be referring to it in a bit more detail for some other topics, so if you wanted to get it handy. Okay. There was noted in the Grant Thornton Report that Hydro has struck a new division of, which is the IS&T Department, that would have been struck in 2000.

MR. ROBERTS: It's not a separate division.

MR. KENNEDY: Okay.

MR. ROBERTS: It's the new department that combines our Telecontrol and what we refer to as MIS, which was our Management Information Systems Departments into one, and it's now called IS&T, Information Systems and Telecontrol.

MR. KENNEDY: Okay.

MR. ROBERTS: So it is a new department that falls underneath the Vice-President of Production.

MR. KENNEDY: Would the establishment of a new department by Hydro have an impact on how the costs associated with, say, a given employee with Hydro that worked in one department at one point and now works with the IS&T Department, would that have an impact on the tracking of costs from year to year?

MR. ROBERTS: Looking back at history, when you're comparing, if you don't know that that change has taken place, you may find that costs in a particular division have gone up or down and I think there are some examples of that because I think if you go back far enough into some of these reports, the old Management Information Systems used to be in Finance and then it got moved, so, and I think Mr. Brushett through the Grant Thornton Reports has indicated at times that there has been some of these organizational changes that have taken place, and what we have endeavoured to do is that, because of the old system, but even with our new system, we're able to re-state so that you can have a comparative basis on a go-forward basis so that you can literally go in and take all these costs in those particular centres and reclassify the history so that you can do on a comparative on a go-forward basis.

MR. KENNEDY: Okay. So Grant Thornton has noted, for instance, that there's been a number of code of account changes made in the year 2000 which affected the way certain costs were tracked for materials and supplies, for instance.

MR. ROBERTS: Yes, there was a change in the way that we reported costs commencing in 2000, and that was directly related to the way that items were coming out of inventory and being recorded to these costs.

MR. KENNEDY: But if you look at the 2001 report at page 29, the second last paragraph commences with the word "increases." "Increases noted in the lubricants, gasses and chemicals account in the Human Resources and Legal Divisions for 2001 and 2002 are due to the account code restructuring introduced in the spring of 2000. All inventory and non-inventory items that fall under the object code gasses, lubricants and chemicals are now recorded to the lubricants, gasses and chemicals account." And I ...

MR. ROBERTS: Yes.

MR. KENNEDY: That's one for the accountants obviously. The distinction fails me but this would be an example of some sort of change in your coding of accounts, that it has an impact on which department gets associated with a cost?

MR. ROBERTS: No, it doesn't affect the department. Just it affected where the accounts were being reported.

MR. KENNEDY: Okay.

MR. ROBERTS: So they're still correct within the department except now instead of being down in lubricants, gasses and chemicals down in miscellaneous, now it's up into materials maintenance.

MR. KENNEDY: Okay. There was one oddity at the bottom of that paragraph in addition to the code restructuring, roof repairs scheduled for 2001 and 2002, to Hydro Place that account for another portion of the increase in Human Resources and Legal Division, and I don't know if there's any significance to the fact that the Legal Division needed a new roof, but ...

MR. ROBERTS: If I may, the Human Resources and Legal Division have responsibility for Materials Management and within Materials Management they have responsibility for Hydro Place.

MR. KENNEDY: So they may not have been necessarily at fault for why there needed to be a new roof, just ...

MR. ROBERTS: That's right.

MR. KENNEDY: ... associated with the cost of it.

MS. GREENE, Q.C.: I need a new (inaudible).

MR. KENNEDY: And there's been a number of questions to some of the witnesses concerning the tracking of some of these costs, as you're aware, Mr. Roberts, and, for instance, if we could look at **RH-1**, Mr. O'Rielly. It was an exhibit that was passed out. As I understand it, the RH-1 was the original production of the net operating expenses and in the comparison of 2001 to 2002 but then when there was an attempt to try to compare these figures to 2001, the evidence of the Hydro witness was, well, they're not comparable, apples to apples, because there's been a number of code of account changes, and so then there was a filed **RH-2**, and I wonder if we could just go to that, Mr. O'Rielly. And this was an attempt to do a reconciliation of some of the code of account changes ...

MR. ROBERTS: That's correct.

MR. KENNEDY: ... that impacted those figures?

MR. ROBERTS: Yes.

MR. KENNEDY: And if I'm gathering correctly from RH-2, the impact of those code of account changes, just so we're clear, it's not additional expense, it's just the reallocation of expense.

MR. ROBERTS: Just a different method of where they are being reported rather than down to the other accounts.

MR. KENNEDY: And that the amount of the reallocation was $1.4 million.

MR. ROBERTS: That's correct.

MR. KENNEDY: And so from that perspective the impact of $1.4 million was 17 percent of the total balance for that particular expense item under that line. It's a fairly significant change that this change in code of accounts had on the expenses associated with system equipment maintenance, for instance, agreed?

MR. ROBERTS: Oh, yes.

MR. KENNEDY: Yeah.

MR. ROBERTS: Certainly increase ...

MR. KENNEDY: And similarly **DWR-1**, given a similar analysis for the TRO ...

MR. ROBERTS: That's correct.

MR. KENNEDY: I don't think that's ... **DWR-5**, I'm sorry, Mr. O'Rielly. And that in this case the code of account change to the TRO system equipment maintenance was $1.76 million.

MR. ROBERTS: Yes.

MR. KENNEDY: And that was 20 percent of the overall balance of the actual account. So these code of account changes may not be just minor or insignificant in nature but could have a dramatic impact on the total costs associated with a particular department. And you'll agree with me then that it makes it very ...

MR. ROBERTS: If I may ...

MR. KENNEDY: Yes, yeah.

MR. ROBERTS: ... it didn't change the total cost by the division or maybe not even by their department, it just changes to where they were disclosed by that department.

MR. KENNEDY: Absolutely.

MR. ROBERTS: So ...

MR. KENNEDY: But it makes it exceedingly difficult, you'll agree, to compare the 2001 TRO system equipment maintenance to the 2000 unless you're aware of this change that's been made to the code of accounts.

MR. ROBERTS: Yes.

MR. KENNEDY: Okay. I'm wondering from a process sort of oriented perspective, process for the application itself, wonder if there's a method that could be employed by Hydro that would, from this perspective, from tracking costs from year to year so that those comparisons can be easily made, whether it's appropriate for Hydro to keep some sort of base year and then following which any changes to the code of accounts that would impact on the allocation of costs from within different departments could be ignored for at least the purposes of looking at what the overall costs are for a full department. Is that possible?

MR. ROBERTS: I guess my comment would be is that this is not a normal item that we have done. This was driven by the situation of, with the implementation of our new systems. We were finding in the case of property maintenance, we had items in our inventory that were used both for maintenance in a particular operating plant as well as on our property, i.e., our buildings and grounds and things like that. The problem that we ran into is that the inventory system is coded to go to one account. The only other alternative was that every time a transaction and a piece of plywood, as an example, came out, somebody had to keep overriding the system and spending that manual effort to change the account code, so the simplest way was for us to go the way that the system was designed and move these things to Materials Management and put them into Materials Maintenance in those particular sections. The availability to a business unit manager who has responsibility for these items doesn't change what he has as control to do this because of the fact that he will raise work orders to track these costs. So from a control perspective there is nothing lost. What comes up in this particular case is that the report that's produced didn't re-state or estimate what the re-statement would be for '97 ... well, '97 wasn't affected ... '99 or 2000. With hindsight, that could have been done, but I think the point is you have to stop somewhere ...

MR. KENNEDY: I appreciate that.

MR. ROBERTS: ... and we can't keep looking back and saying what if, because the longer it goes the harder it becomes, so you have to adopt the change and if you can re-state to make it comparable, that's fine; if you can't, but you got to cut the cord.

(10:45 a.m.)

MR. KENNEDY: And your own professional opinion, what's a reasonable period of time in which you would consider to be a review period for doing a year-to-year comparison, a three-year period, a five-year period?

MR. ROBERTS: I'm not sure I follow what you mean by doing a review.

MR. KENNEDY: Well, put it this way, if I wanted to compare 2002, well say that Hydro does come back in 2003 and you're looking at the expenses and you're looking at 2002's expenses and you want to compare them to previous years, would a, from your professional position, would a looking back three-year period be appropriate, a five-year period, for a company such as Hydro?

MR. ROBERTS: I don't think there's a magic rule as to what it would be. I think it's a judgement call in all cases as to how far back history will help you. It may be used as a guideline. Back two or three years ... once you start moving outside of the two or three years, you're getting stale data. It's the same thing as moving forward, trying to guess out past one or two years ...

MR. KENNEDY: Looking back in 1992 provides little assistance, for instance, to everybody potentially.

MR. ROBERTS: It gives you some information but how valuable that is to you ...

MR. KENNEDY: Sure. But what I'm ... when Hydro is there in 2003 and one were to look back at 2002 expenses and compare them to, try to compare them to 2001 and 2000 and 1999, for instance ...

MR. ROBERTS: I wouldn't be going back. I wouldn't be going back past 2001 because, as I say, you're getting old information.

MR. KENNEDY: But that's only one-year comparison then, 2001 to 2002.

MR. ROBERTS: Well, you would have 2001, 2002. You would have 2003 and ...

MR. KENNEDY: Wait a minute.

MR. ROBERTS: ... (inaudible) 2004 ...

MR. KENNEDY: The 2003 ...

MR. ROBERTS: ... is the test year.

MR. KENNEDY: Okay. The 2003 would be an estimate. So if I wanted to compare ...

MR. ROBERTS: Depending on your point in time ...

MR. KENNEDY: If I wanted to compare ...

MR. ROBERTS: ... it may reflect some actuals as well as a ...

MR. KENNEDY: There may be a pro forma ...

MR. ROBERTS: ... forecast for the balance of the year.

MR. KENNEDY: But if I wanted to review complete actuals for completed financial years, I would have 2002, 2001, so I'd only have one-year comparison, which would be two dots on my graph, going to be a straight line but it's not going to really show me a trend, is it?

MR. ROBERTS: Well, if you go back, 2000 will be comparable to 2001.

MR. KENNEDY: Right, okay.

MR. ROBERTS: Okay. So ...

MR. KENNEDY: But are there code of account changes being made by Hydro in 2001, for instance, that are going ...

MR. ROBERTS: No.

MR. KENNEDY: ... to make it difficult for me to compare it to 2000?

MR. ROBERTS: Not that I'm aware of.

MR. KENNEDY: So the department change of the IS&T, for instance ...

MR. ROBERTS: Doesn't change the reporting.

MR. KENNEDY: Okay.

MR. ROBERTS: All the IS&T as a department is still intact, so if you said to me you want to look at IS&T costs last week, last month or two years from now, the way that the accounts are structured in the business unit, that information can still be hauled together no matter where it's reporting and provided to you as a particular department.

MR. KENNEDY: Okay. So in 2003 there should not be any difficulty in comparing 2002 to 2001 to 2000, insofar as code of account restructuring is concerned.

MR. ROBERTS: As of this point in time there is no plans, and believe me after going through this one, I'll be hard-pressed to make another change, there is nothing planned that would warrant a change from the way that we're reporting right now, and we should be able to, if we're here in 2003, go back to at least 2000 on these particular accounts and compare the same things, and some of the other accounts you can, would be able to go back longer. It's just a function of what accounts were affected.

MR. KENNEDY: Okay.

MR. ROBERTS: Like, for instance, if I may, the travel account, it's still travel. It hasn't been changed.

MR. KENNEDY: Yeah.

MR. ROBERTS: And it's unfortunate that these were there but they were done for an efficiency reason of having to, do you re-code 50,000 part items every time you take an item out of inventory or do you leave the system intact and let it flow through, because you do have a (inaudible) system that is able to still be able to track the costs for you if you so desire.

MR. KENNEDY: And if circumstances changed and Hydro decided that for its own purposes of efficiency, operational or otherwise, that it needed to make a code of account change from some point subsequent to this date, that, if I'm gathering you correctly, it wouldn't be an undue burden to place on Hydro to ensure that it was able to track the changes so that in 2003 it would still be, parties would still be able to make comparisons from 2002 to 2001 and 2000.

MR. ROBERTS: As long as there is a cut point, that you don't keep doing this forever, what if.

MR. KENNEDY: So, and that's why I was asking you about the periods of time which you would consider in your professional opinion to be a reasonable amount of time to do those year-over-year comparisons, three years, five years. Where would you want ...

MR. ROBERTS: That's what I say, it's difficult to be that precise. It's really a function of the costs that you're looking at and what it really means.

MR. KENNEDY: What, the costs it's associated with.

MR. ROBERTS: Yes.

MR. KENNEDY: Okay. Chair, that's probably an appropriate time to break. I'm just about to start another topic and I don't think I'd get through it in six minutes, so ...

MR. NOSEWORTHY, CHAIRMAN: Thank you. We'll reconvene at 10 after.

(break)

(11:10)

MR. NOSEWORTHY, CHAIRMAN: Thank you, very much. Mr. Kennedy, do you still have some questions on your cross-examination?

MR. KENNEDY: Yes, Chair. It's just a couple of more topic areas, Mr. Roberts. The first thing I wanted to just cover with you is the issue of professional fees. And I think a good place to start there is the Grant Thornton 2000 report, Mr. O'Rielly, and specifically, page 21. Page 21. Actually, if you can flip back to just page 20 first. The last paragraph on page 20, Grant Thornton noted that the professional services expense category has exhibited a significant upward trend over the past four years, 64 percent increase from 1996 to 2000, and then over on page 21 is the list of expenses for during 2000, and I realize that you're not directly responsible for the budget perspective for professional fees, outside of your own department, that is?

MR. ROBERTS: That's correct.

MR. KENNEDY: But you'd acknowledge, would you, that a 64 percent increase in professional fees from 1996 to the year 2000 would require some scrutiny and raise some questions as to the costs associated in this particular budget item?

MR. ROBERTS: Yes.

MR. KENNEDY: And would you agree with me that in the case of the professional fees that many of the items in, for instance, this year 2000 are discretionary in nature? In other words, they're one offs, they're projects that were completed in the year 2000 but won't be repeated in 2001, for instance?

MR. ROBERTS: Some of those projects are in that category but there are some ...

MR. KENNEDY: Some are ongoing ones?

MR. ROBERTS: Some are ongoing. As an example, the second one on the page, the audit services.

MR. KENNEDY: Right. Or the annual report fees?

MR. ROBERTS: Will continue on. You'll find the same thing in production when you're dealing with the monthly consulting services at Holyrood, but there will be some that will come up one year that won't be there the next year, but they may be replaced by something else.

MR. KENNEDY: The Hydro strategic planning initiative, for instance, may be a discretionary item in that it's not likely to be repeated again in 2001?

MR. ROBERTS: That's correct.

MR. KENNEDY: And the TRO proposal for a management environmental system of $28,000 or a proposal for an environmental audit system of $28,700 are discretionary items in the sense that they're not likely to be repeated in 2001?

MR. ROBERTS: Similar costs may not be repeated in 2001, but as a result of those you may trigger additional costs in the environmental area. It may not be a professional service, though.

MR. KENNEDY: Right. Can you tell me, you, as the Controller of Hydro, do you feel that there are adequate budgetary controls in place to ensure that the professional fees are kept under control and that any unnecessary costs are being voided in this particular expense item?

MR. ROBERTS: In my opinion, based on the review process that we have in place, then it is justifying these particular costs as they come up through the ranks within the various divisions, and then eventually to the management committee during their review in June of each year. Management still reserves that final decision, even though those reviews have been done in the individual divisions up to and including the vice-president level. Management still reserves and does exercise that right to question the level of cost there and whether or not there is still a possibility that some items can be shifted from one year to a next, the same as it would do with just about any costs that's within a particular budget.

MR. KENNEDY: And so within these expenses there would be issues as to, for instance, whether to complete a project in a particular year as opposed to postponing it for another year, or whether a study could be done by internal resources as opposed to being hired by outside consultants, that they're issues that need to be determined in ...

MR. ROBERTS: Most of those issues would be determined well before the management committee, would be back to the business unit level of saying do we have the internal resources to do this, do we have the expertise in the house to do it, and if we don't and if it's still required then we have no other choice but to go outside.

MR. KENNEDY: So would you, as a controller, have any involvement in scrutinizing these costs and determining their appropriateness or providing indications to management that this particular budget item has seen a fairly significant increase in the period 1996 to 2000?

MR. ROBERTS: I have access to all this information at every single business unit level. In the presentations that are done to the management committee for budget reviews the budget reviewing information shows, first of all, the corporation as a whole, which is very similar to what you're seeing in my revenue requirement of looking at professional services for the Company in total. And we would provide commentary saying, as an example, that if professional services went up $1 million, here's the contributing factors that we could determine caused that, so at that very high level of report it's done to the management committee to get their attention towards the issues that we have identified. Once that is done ... and that presentation could be anywhere from an hour to two hours, could be half an hour, depending on the issues that are being raised in our high level summary that we would provide. The management committee then will review each division by itself and avail of that opportunity to have the vice-president justify as to why these particular costs are to be recorded for this particular year.

MR. KENNEDY: So is that a top down initiative? In other words, do you, as controller, track the expense item and when you note a significant increase year over year or over a period of years initiate a cautionary note, if you will, to management about that?

MR. ROBERTS: Well, the reporting would provide some history, going back at the previous year or maybe two years, plus your budget, so that information is what we would be advising management on and they would have that report. We would just add a commentary to it, based on our findings at a high level, as to here are some of the contributing factors to this particular increase in cost for this year.

MR. KENNEDY: I guess what I'm trying to get at, is do you, as a controller, troll around the finances of Hydro and try to pick out areas which may be of concern to management in that the increase is significant year over year, over a period of years?

MR. ROBERTS: Do I raise issues, yes.

MR. KENNEDY: Yes, okay.

MR. ROBERTS: I do.

MR. KENNEDY: And would this be an example of an issue that you may raise as Controller that the professional fees of Hydro have increased significantly as noted by Grant Thornton during that period?

MR. ROBERTS: Well, I may be raising it in a different vein. I may be raising it from the point of view of, to management saying, for your information, included in this year's cost is this project that you should be aware of, and I may express my own opinion to management committee, which I will do, as to whether or not, you know, if I have an opinion on it whether or not I think, in my mind, there may be an option or an alternative to delay or whatever.

MR. KENNEDY: So is there ...

MR. ROBERTS: So I'm not restricted in my comments, to date.

MR. KENNEDY: No, fair enough. Is there a report, specific report that you issue on an annual basis of your analysis of Hydro's expenses ...

MR. ROBERTS: No.

MR. KENNEDY: ... in trying to earmark areas that may bear more scrutiny?

MR. ROBERTS: In the information that we would provide to management, in June of each year, would be the various budget reports that they would look at and we would provide a high level commentary looking at the corporate numbers in total. For instance, if professional services had increased by $1 million we would highlight up front in that commentary, what contributed to that particular increase.

MR. KENNEDY: I'd just like to move on to just another topic, and assistance would be Schedule 1-A filed October 31, 2001, Mr. O'Rielly, and the line that I'm interested in is line 39, Mr. Roberts, which is the interest expense line in your revenue requirement.

MR. ROBERTS: Yes.

MR. KENNEDY: And when you look at the variance for 2002 between the as filed and these revised figures as per October 31 the lone item of interest is the largest number of them all, if you will, on the variance from between what was filed originally and what's being filed as of October 31, and the footnote 27 provides the explanation of that, and the net of one ... the stated figure of $1,763,000 is actually a net of a number of things?

MR. ROBERTS: That's correct.

MR. KENNEDY: And one of them is the decrease mainly due to lower interest rates, $2,280,000?

MR. ROBERTS: Yes.

MR. KENNEDY: Could you, first, just give me an explanation of and sort of a general view of why the interest rate is lower by $2,288,000?

MR. ROBERTS: Our treasury department, in redoing the 2001 and the 2002, used more current information on interest rates, and based on those new rates, combined with changes in cash flow arising from a more up-to-date situation in 2001 resulted in that decrease in interest expense.

MR. KENNEDY: So it's a combination of lower interest and, presumably, improved cash flow?

MR. ROBERTS: There's a change in the cash flow and there's a change in interest rates, and there was also a decision made that in the original application we were going to have a total long-term debt issue of a total of $300 million. In the revised we are going with $250 million long-term and keeping an extra ... shouldn't say an extra. Keeping part of the $50 million that was originally planned to go long-term as short.

MR. KENNEDY: Okay.

MR. ROBERTS: So that has also contributed to the reduction in the interest rate.

MR. KENNEDY: And that decision, I take it, is borne in part by the lower interest rates on short-term money?

MR. ROBERTS: That was all items that were considered by our treasury department when they were redoing their interest drawn and their financing proposed for 2002.

MR. KENNEDY: Just to follow-up then with a question in one of the earlier areas that I covered regarding the $300 million cap on the Hydro short-term borrows.

MR. ROBERTS: Yes.

MR. KENNEDY: Is there, as far as you're aware, been any initiative either taken or contemplated by Hydro to increase that cap to request government to increase the $300 million cap on short-term borrows?

MR. ROBERTS: I'm not aware of any request to increase the cap.

MR. KENNEDY: Okay. As a controller of the Company would you, if that cap was increased from 300 million to some greater figures, would that provide Hydro with greater flexibility on its short-term borrowings than it presently has?

MR. ROBERTS: I guess it's an area that's difficult for me to answer because I'm not involved in the day-to-day operations, and the planning and the information that's done through treasury looking at future market conditions, future interest rates, where's our current cash position ...

MR. KENNEDY: That would be a question for Mr. Osmond, perhaps?

MR. ROBERTS: You can put it to Mr. Osmond because the treasury reports to him the same as I do.

MR. KENNEDY: Alright, we'll get Mr. Osmond to answer that one. I'm wondering though if you could ... in response to **NP-81** Hydro provided some detailed calculations on the interest rate projects for 2001 and 2002?

MR. ROBERTS: Yes.

MR. KENNEDY: I'm wondering if this **NP-81** could be revised to reflect the new interest as per your October 31, 2001 filing?

MR. ROBERTS: Yes, it can.

MR. KENNEDY: Okay. I wonder if I could have that undertaking, counsel for Hydro?

MS. GREENE, Q.C.: Yes. That won't be available today.

MR. KENNEDY: No, that's fine. I understand.

MS. GREENE, Q.C.: If there's questions Mr. Osmond could respond to them.

MR. KENNEDY: Okay, that's fine. Thank you. Similarly, **NP-87**, Hydro, in response to a question, provided details of the calculation of its interest expense for 2002, identifying the long-term debt by issuing the applicable short-term debt?

MR. ROBERTS: Yes.

MR. KENNEDY: And this is a particularly difficult document to look at in electronic form. It's almost like a big blur. The hard copy is marginally better as the numbers are rather small, but could you in turn provide a revised calculation of the interest expense tying into the total of $9,821,000 at line 39 of that Schedule 1-A, the calculation pursuant to **NP-87**?

MR. ROBERTS: So you want **NP-87** revised ...

MR. KENNEDY: Revised.

MR. ROBERTS: ... to reflect. I don't see any difficulty in providing that.

MR. KENNEDY: Okay. If we could get that, as well, Counsel?

MS. GREENE, Q.C.: Uh hum.

MR. KENNEDY: Thank you. Just while we're on interest, Mr. Roberts, there's been some questions referencing this regulated interest coverage calculation and that's, as I understand it, one of the calculations is tied to the cost of service?

MR. ROBERTS: That's correct.

MR. KENNEDY: Will you agree with me though that that regulated interest coverage calculation is a product of how Hydro used to be regulated on interest coverage?

MR. ROBERTS: That's correct.

MR. KENNEDY: And that going forward that really the only relevant interest coverage calculation is the one that the bond rating agencies use themselves? Is that fair to say?

MR. ROBERTS: No. I still think Hydro, as a corporation, will still calculate and continue to calculate an interest coverage. It does not report this regulated interest coverage except to the Public Utilities Board, but it does calculate a corporate interest coverage, and I see absolutely no reason why we wouldn't continue to do that. From a regulatory perspective, the calculation of a regulated interest coverage is ...

MR. KENNEDY: It's no longer relevant?

MR. ROBERTS: It's not relevant. It's something that could be done if the Board so decided that it would like to have it, but it's not a requirement. The key now is that return on rate base because that's really what controls the situation.

MR. KENNEDY: I have a couple of questions, Mr. Roberts, on non-regulated expenses, and Ms. Butler reviewed some of these items with you. I have though a couple of other questions. One relates to Hydro's corporate communications plan. I wonder if we could turn to **NP-286**, Mr. O'Rielly?

MR. ROBERTS: $75,000.

(11:30)

MR. KENNEDY: And the question was in reference to page 135 in the report of Grant Thornton, LLP, on Newfoundland and Labrador Hydro's 2001 rate hearing. "In your opinion, should the communication plan advertising of $75,000 be a regulated cost or is the nature of the plan one of corporate promotion, and therefore, should be chargeable to non-regulated accounts." And the reply by Hydro was "It is our understanding," which I'm just curious why, any idea why it would be phrased "It is our understanding" seeing how it's Hydro's communication plan that's ...

MS. GREENE, Q.C.: It's not actually a reply of Hydro.

MR. KENNEDY: Oh, I beg your pardon. This was a reference to Grant Thornton?

MS. GREENE, Q.C.: Yes.

MR. KENNEDY: I'm sorry. Right, okay, so that's where I got turned around, but the reply then by Grant Thornton was that the purpose of the communication plan is to strengthen Hydro's corporate image with their external and internal stakeholders, effectively communicate internally and externally, enhance employee effectiveness and build closer relationships with communities and their customers, and then ... so that's correct. In Grant Thornton it says, "In our opinion, the nature of the communication plan is one of corporate promotion and should be considered a non-regulated expense." As the controller responsible for tracking regulated versus non-regulated expenses, Mr. Roberts, I'm wondering if you agree with that position and whether you would agree that the corporate communication plan should be treated as a non-regulated expense?

MR. ROBERTS: I guess the issue is whether or not you consider changing our relationships with our customers to be an enhancement of corporate image or if it's designed towards and awareness of who Hydro is and what it does, so I guess I'm looking at it from the point of view, and I know I'm not answering your question directly, I look at it, from my perspective, the final decision is going to be made by this Board on this $75,000 item. Through the whole strategic planning process in Hydro it has been identified that communications, even among our own employees, do need improvement, and employees have expressed that to the corporation. This cost of $75,000 is to provide some assistance from a consultant in how we can change that and also recognize that Hydro has to increase its level of understanding with some of its various customers relative to the communities in which we serve as to what Hydro is, what it does, and fully understand that issue.

MR. KENNEDY: Okay. You'll agree with ...

MR. ROBERTS: So it's not to be sponsoring the six o'clock news or the seven o'clock NTV news, or whatever the case may be. It's an awareness primarily aimed towards our own employees understanding more about the organization and how it works and also to enhance our relationship with our customers too.

MR. KENNEDY: Okay, so clearly it doesn't deal directly with safety?

MR. ROBERTS: Safety will probably be part of it.

MR. KENNEDY: Indirectly?

MR. ROBERTS: I guess at this point, until the study is done, and I don't know what the results are going to be, but safety in the communication plan that will be developed out of this. Safety would certainly be one of the aspects of it, are we doing the right things in the right times and communication and the word there.

MR. KENNEDY: For instance, in your advertising expenditures, the Hydro advertising, there's an RFI which provides a rather lengthy list of ...

MR. ROBERTS: 188 pages.

MR. KENNEDY: Of every advertising place by Hydro, and was there any attempt to go through that in electronic form to determine what advertising was, corporate primping, if you will, versus what advertising was for safety or reliability or the provision of electricity?

MR. ROBERTS: Historically in Hydro we have not advertised. The majority of those costs in that are to deal with planned outages, notices of things happening along that lines, advertising for staff. It has not been a pure advertising, in my mind. There may be the odd cost in there for putting a notice in the paper saying this is safety week, the same as most other companies would do, and here is the power commitment or whatever the safety message is for that particular year, but the majority of those costs would be directly related to operations.

MR. KENNEDY: Okay, but if I'm gathering correctly, there's no ... and I think this has been established, a written policy in place that would guide you, as a controller, in making a determination on an expense by expense item, like, for instance, the communications plan item of $75,000 to determine whether it should be booked as a non-regulated versus a regulated expense?

MR. ROBERTS: There's no written policy. The incurance of that cost would go through the still budget proposal, operating budget scenario and would go to management, and the decision, unless so ordered by the Board, or unless Hydro internally itself decides that we feel this is not a regulated cost, then it would just go through the same as any other cost.

MR. KENNEDY: And that's done on a discretionary basis just applying your own unwritten rules about what should be treated as a regulated versus a non-regulated expense?

MR. ROBERTS: I think some of these are sort of like straightforward issues ...

MR. KENNEDY: Some of them speak for themselves?

MR. ROBERTS: The grey issues would be discussed, either within a division or raised to management.

MR. KENNEDY: Just one further question on the non-regulated expenses. This is an item that shows up annually in Grant Thornton's annual reports, Mr. Roberts, and I wonder if I could just get your comment on it. It's a small item, but one that seems to be going unaddressed by Hydro, and if you turn to Grant Thornton's 2000 report, Mr. O'Rielly, on page 22? It's in the paragraph just before equipment rentals, and it's "Similar to our 1999 findings we noted during our review of the travel accounts that management travel include several payments for spousal travel costs. While these items are accepted practice by Hydro, we believe that it's not prudent to include expenditures of this nature in the revenue requirement." And that was noted again at 2001, so it's an expense that was booked by Hydro as a regulated expense in 1999 and then again in 2000 and again in 2001 despite these comments by Grant Thornton, so I'm wondering if you could provide an explanation as to why the Grant Thornton recommendation is being ignored in this regard?

MR. ROBERTS: We don't budget specifically for this particular type of cost, but we, as a corporation, recognize that it may happen and it probably does, as you can see from this report, and we haven't adjusted the revenue requirement by that amount.

MR. KENNEDY: But can you tell me why, despite Grant Thornton's comments in 1999, 2000 and 2001, there hasn't been an adjustment made by Hydro to ensure that spousal travel costs are not part of the revenue requirement?

MR. ROBERTS: All I can tell you at this point is that we haven't made an effort to identify those costs and eliminate them.

MR. KENNEDY: The last item I have, Mr. Roberts, is just a very brief one concerning the contingency fund. You received some questions from counsel about the use by Hydro of the contingency fund, and there was a question concerning what its original purpose was, and for your assistance I've gotten an excerpt from a Board decision **PU-31**, 2000, 2001. And if I gathered correctly, Mr. Roberts, you seemed to be, at the time, a bit unclear as to what the direction was by the Board concerning the use of the contingency fund, or is that an unfair statement? And I guess I'm drawing to your attention now **PU-31**, and I'm wondering ... and at paragraph 7 of **PU-31** the direction of the Board was, "As part of its quarterly capital expenditure reports to the Board in 2001 the Applicant will provide an itemized listing of the amounts allocated to the contingency fund, including a description of the projects, the amount spent on each project, any future commitments and the reasons why there was an exigency requiring the use of funds." Does that improve your understanding of what the purpose of the contingency fund was and under what conditions it was to be used by Hydro?

MR. ROBERTS: That was my understanding of the reporting mechanism that was put in place based on the order that was obtained on the 2001 capital budget.

MR. KENNEDY: And that the contingency fund is to be used for, not for purposes of discretionary projects, but to be used for projects that are required to be used, that would be implied by the exigency requiring the funds, the conditions under which why these funds are being required to be used?

MR. ROBERTS: Yes, and full reporting, as I understand it, is being done to the Board for the items that are being used there.

MR. KENNEDY: I have one more question, sorry, Mr. Roberts. There was some testimony about the billing relationship between Hydro and Newfoundland Power, and this was on the lead lag analysis?

MR. ROBERTS: Yes.

MR. KENNEDY: And your counsel provided an indication to the Board that there was, in fact, no written contract in place between Hydro and Newfoundland Power at the present time and that there's been a continuation of the agreement between the two parties and there is an undertaking outstanding regarding what that understanding is. From a controller's perspective, this is a client that Hydro bills a total of some $270 million in the run of a year?

MR. ROBERTS: Yes.

MR. KENNEDY: It's your one biggest customer?

MR. ROBERTS: Yes.

MR. KENNEDY: It constitutes 70 percent of your total revenue?

MR. ROBERTS: Yes.

MR. KENNEDY: Would you, as a controller, consider it appropriate to bill a customer of that size on a more frequent basis than monthly?

MR. ROBERTS: Would I consider it? Consideration could certainly be given, but it would have to be in consultation with our customer as to what's required. The actual invoicing to Newfoundland Power is not just one piece of paper. There are multiple meter readings that have to be obtained, calculations that have to be done in order to be able to provide that information to ... provide that billing to Newfoundland Power.

MR. KENNEDY: If the billing by Hydro to Newfoundland Power was done on a more frequent basis it would decrease the revenue lag, correct?

MR. ROBERTS: Depending on what the terms of payment are as well. It's not just a simple matter of billing it.

MR. KENNEDY: If the payment terms were in lock step with the billing terms?

MR. ROBERTS: It would have an impact on the revenue lag.

MR. KENNEDY: And if it ...

MR. ROBERTS: If it could be increased.

MR. KENNEDY: ... decreased your revenue lag it would decrease your working capital requirements, correct?

MR. ROBERTS: Yes.

MR. KENNEDY: And that would decrease your revenue requirement?

MR. ROBERTS: Yes.

MR. KENNEDY: Those are all the questions I have, Chair. Thank you, Mr. Roberts.

MR. ROBERTS: Thank you.

(11:45)

MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr. Kennedy. Thank you, Mr. Roberts. We'll move now directly to Hydro on redirect, Ms. Greene.

MS. GREENE, Q.C.: Thank you, Mr. Chair, and at this time I will provide the list of undertakings from yesterday, because I plan to take Mr. Roberts through those and address them at this time.

MR. NOSEWORTHY, CHAIRMAN: Yes.

MS. GREENE, Q.C.: There were four undertakings provided yesterday, and in the course of redirect we will be addressing all four, so I do not plan to speak to them at this time. Mr. Roberts, counsel for Newfoundland Power asked yesterday with respect to the balances for inventory in each of the months from December 2000 to present. Have you had that prepared since yesterday?

MR. ROBERTS: Yes, I do.

MS. GREENE, Q.C.: And I have a copy of that to distribute at this time, as well, and in terms of marking this, Mr. Kennedy, would it be an undertaking or an exhibit? It is in response to an undertaking to Ms. Butler.

MR. KENNEDY: We should perhaps label it then as an undertaking so we can keep track of it, Counsel. That would be **U-Hydro** number, I'm not sure. I'll wait for the Board Secretary. That's **U-Hydro No. 25**, Counsel.

EXHIBIT U-HYDRO NO. 25 ENTERED

MS. GREENE, Q.C.: Mr. Roberts, could you just please explain the schedule that's been distributed?

MR. ROBERTS: Yes. What we've done overnight is that we've gone back through the financial records and identified the supplies inventory balances starting in December of 2000 and coming all the way forward and including October of 2001. This represents only an 11 month average rather than a 13 month average, which is what's being used in the calculation of the rate base, but as you can see, based on the 11 months of results, using actual information, the average is approximately $20.8 million versus what we had used in the calculation, a rate base of 21.1. It would not be unusual for Hydro over the next couple of months to be increasing its inventory slightly as a result of ensuring that adequate supplies are on hand because of the winter season.

MS. GREENE, Q.C.: In your opinion, would it be necessary to adjust the amount included in the 2002 forecast for supplies inventory?

MR. ROBERTS: In my opinion, I wouldn't require any further adjustment.

MS. GREENE, Q.C.: And that's because you expect the balance to increase in the next two months, is that correct?

MR. ROBERTS: I would expect that the inventory will change over the next couple of months.

MS. GREENE, Q.C.: The second area for questioning, Mr. Roberts, concerns an undertaking, again, given to Ms. Butler, and it related to the revised calculation of employee future benefits for 2001 and 2002, and I have a schedule for that to distribute at this time, as well.

MR. KENNEDY: Chair, that would be **U-Hydro No. 26**.

EXHIBIT U-HYDRO NO. 26 ENTERED

MR. NOSEWORTHY, CHAIRMAN: Thank you.

MS. GREENE, Q.C.: Mr. Roberts, now that everyone has a copy of that could you just please briefly outline what is shown on **U-Hydro No. 26**?

MR. ROBERTS: Yes. In an earlier RFI, based on the original filing on a request from Newfoundland Power, we had provided information on the components making up the employee future benefits account that was recorded on the balance sheet. In the revision for October 31 some of these numbers were updated, as well as to make a correctION for interest, so on the schedule what we have done is shown the individual year showing the as filed and what the revised amounts now represent.

MS. GREENE, Q.C.: The third area for question on redirect, Mr. Roberts, arises from an undertaking given to Mr. Hutchings, and it related to the mill rate to the industrial customers arising from the RSP adjustment. Now that the September 30th balance is available have you had time overnight to determine that?

MR. ROBERTS: Yes, we have.

MS. GREENE, Q.C.: And again, I have a schedule at this time to distribute in response to that undertaking.

MR. KENNEDY: **U-Hydro No. 27**, chair.

<u>EXHIBIT U-HYDRO NO. 27 ENTERED</u>

MR. NOSEWORTHY, CHAIRMAN: Thank you.

MS. GREENE, Q.C.: Again, Mr. Roberts, would you please explain what **U-Hydro No. 27** outlines?

MR. ROBERTS: The **U-27** outlines the status of the Rate Stabilization Plan for the industrial customers as of the end of September. Their balance and the calculations of mill rate is based on the September balances rather than December 31, which is what Newfoundland Power would be. Their share of the plan, as of September the 30th, 2001 is approximately $18.8 million. One third of that balance will be recovered over the period commencing January the 1st, 2002, and based on the sales in gigawatt hours that translates into a mill rate of 5.14 mils that will become effective January the 1st of 2002.

MS. GREENE, Q.C.: The next question for you, Mr. Roberts, arises from an undertaking provided to counsel, Mr. Hutchings, for ... and it related to the payment terms with Newfoundland Power. Can you please advise the Board of what the practice has been with Newfoundland Power for the payment of its invoices?

MR. ROBERTS: Yes. The practice with Newfoundland Power is that their account is paid around the 20th of each month.

MS. GREENE, Q.C.: I'd like now to turn to the 1985 PUB report, which you will find under **CA-No. 6**, and you do have to go to the hard copy for this. Yesterday, in questions from the Consumer Advocate, Mr. Roberts, you acknowledged that Hydro proposed the Rate Stabilization Plan at the 1985 hearing, is that correct?

MR. ROBERTS: Yes, I did.

MS. GREENE, Q.C.: And I guess Mr. Browne asked you to read certain references but he didn't ask you to read the ones as to why Hydro was proposing it, and I'd like, for the record, that we look at those. The first is at page 39 which outlines what Hydro's submission on the Rate Stabilization Plan was. I wonder, for the record, if you could read in the first, well, certainly the first two sentences in the first paragraph, please?

MR. ROBERTS: "Mr. Avery (phonetic) testified that Hydro is proposing that a Rate Stabilization Plan be established to replace the present water equalization provision. This plan will help ensure that rates remain stable and certain over the next two to three years. In addition, it will ensure that consumers will benefit should favourable events result in significant improvement in Hydro's financial position."

MS. GREENE, Q.C.: And then you see, Mr. Roberts, that there is a description of what you also explained yesterday, the water variation provision and the fuel cost variation provision. Would it be correct to characterize those as saying that they provided revenue stability to Hydro for changes in water variation and fuel cost back when they were in existence in 1985 and before?

MR. ROBERTS: Yes.

MS. GREENE, Q.C.: The next page I'd like to take you to is page 42, and I'd ask you to read the first paragraph as shown on page 42?

MR. ROBERTS: Commencing with Mr. Avery

MS. GREENE, Q.C.: Yes, that paragraph.

MR. ROBERTS: "Mr. Avery stated that overall Hydro believes that the adoption of the proposed Rate Stabilization Plan will stabilize rates to customers and provide the certainty that has been missing over the past few years."

MS. GREENE, Q.C.: And that was the Board's description of Hydro's submission with respect to the RSP, and now I'd like to turn to page 87, which is the Board's findings, and here, if you could read the first paragraph on page 87, please?

MR. ROBERTS: Yes. "The FAC varies from month to month and is usually at its highest in the winter months."

MS. GREENE, Q.C.: If I could stop you there. What is the FAC?

MR. ROBERTS: The FAC is the fuel adjustment charge.

MS. GREENE, Q.C.: And can you carry on, please?

MR. ROBERTS: Yes. "The elimination of the FAC will mean that fuel costs will be reflected in higher basic rates and will not vary from month to month between adjustments made for the Rate Stabilization Plan and will protect the consumers from the largest increase in the FAC that occurred during the winter of 1984-1985."

MS. GREENE, Q.C.: To your knowledge, Mr. Roberts, have there been public demonstrations with respect to the electricity prices since 1985 as there were in `84 and `85?

MR. ROBERTS: No, there has not.

MS. GREENE, Q.C.: The last question that I have for you arises from Mr. Kennedy's question on spousal travel, and I wondered if you could advise the Board and the (inaudible) as to the type of spousal travel that we're talking about? For example, do members of the management spouses travel to exotic locations such as the Caribbean?

MR. ROBERTS: No, they do not. My information on this is that at Christmas time it is customary for a member of the management committee to attend a Christmas dinner function in the area offices and the spouse of the particular member of the management committee, or a designate of the management committee, has taken their spouse with them.

MS. GREENE, Q.C.: And those Christmas functions, would employees who live in the region who attend those functions be attending those with their ... I was trying to think of the diplomatic term for spouse ... spouse or significant other.

MR. ROBERTS: Yes, they would.

MS. GREENE, Q.C.: Partner, thank you.

MR. ROBERTS: Yes, they would.

MS. GREENE, Q.C.: So that's the type of spousal travel, is it?

MR. ROBERTS: Yes, it is.

MS. GREENE, Q.C.: Christmas parties or recognition awards?

MR. ROBERTS: That's correct.

MS. GREENE, Q.C.: Thank you, Mr. Roberts. Those are all my questions.

(12:00)

MR. NOSEWORTHY, CHAIRMAN: Thank you, very much, Ms. Greene, Mr. Roberts. We'll move now to Board questions and we'll begin with Commissioner Powell.

COMMISSIONER POWELL: It's hard to be politically correct these days. Well, Mr. Roberts, thank you, very much. You seem to have an understanding of the financial where for all of Hydro.

MR. ROBERTS: Yes.

COMMISSIONER POWELL: I guess the same job for 17 years, there's certain things you pick up.

MR. ROBERTS: I certainly hope that I've been able to provide some of the information that I accumulated over the years to the Board and been of assistance in answering some of the questions.

COMMISSIONER POWELL: Well, the area I want to get at, I'm trying to ... new at the process, new to Hydro. I've been asking the people in the other levels exactly what they do and how it fits in. One of the things that have been brought up, we talked quite a bit about the past number of weeks is the JD Edwards system.

MR. ROBERTS: Yes.

COMMISSIONER POWELL: Could you sort of give me an overview of exactly, in your perspective, what the JD Edwards system is and what it does?

MR. ROBERTS: The JD Edwards is a financial system, computerized system, and it is a fully integrated system, and what I mean by integrated is that the very ... the individual pieces of the system, such as the accounts payable, enters directly through general ledger and also to other systems that are all tied together, so there's one source of information that can be spread among various system. And if I may just to maybe give you an idea of what I'm referring to there when I say integrated, prior to the implementation of the JD Edwards system we had a financial reporting system and we had a maintenance system. To get the information in the maintenance system it had to be entered a second time, so that to maintain maintenance records and work orders, there was a duplication of effort in recording of cost. They would record it through the financial systems report, the payment by a supplier, and go through the cost expense categories that we have, but to track these costs by an individual work order or type of work required duplication of effort of entering this information into another system in order to be able to do it. The JD Edwards system has eliminated that because of the fact that it is a fully integrated system and it uses the ... it doesn't require an interface or anything to be written for one system to talk to another, so within the general ledgers in the JD Edwards system what we have is a basic general ledger system, we have an accounts payable system so we can pay our suppliers, we have an inventory system, we have a purchasing system, we have an accounts receivable system, we have a fixed asset system and we have a job costing system that's used for tracking of work orders on capital. So all of those systems encompass the JD Edwards system, in addition, of course, to payroll, so that there is one source of point of entry that can go to multiple ledgers from the point of view of being able to provide information to various business unit managers.

COMMISSIONER POWELL: But JD Edwards is not an accounting system dedicated just for utilities?

MR. ROBERTS: No, it is not.

COMMISSIONER POWELL: It's a ... so basically what we're looking at is a Cadillac of the (inaudible) system, sort of thing, in a sense of ... in terms of cost analysis and detail and things?

MR. ROBERTS: I think it's a lot further advanced than the (inaudible) as you referred to it.

COMMISSIONER POWELL: Okay.

MR. ROBERTS: I guess I might add, the other system that I forgot to mention to you is that we also ... tying into the JD Edwards suite and done by JD Edwards is the system to look after our 35,000 rural customers, we refer to as our utility customer information system, so the individual billings for all those customers, prior to the implementation of JD Edwards, used to be done outside by Newfoundland Power utilizing a system that they had maintained for us. Now everything is inhouse and it flows, as I mentioned, in the integration. The information is recorded here and it's flowing through and there's no additional work to get the information.

COMMISSIONER POWELL: When did you start doing your change over to JD Edwards?

MR. ROBERTS: The decision to go to JD Edwards was made in late `97, and implementation started in 1998, because of the fact that we were replacing all our systems and adding new ones, and it took all of 1998 and 1999, and coincidental with that was the Y2K issue, as well, so it was doing two things at the same time.

COMMISSIONER POWELL: Okay, so who controls the codes and the software, that's at your department or is that the ...

MR. ROBERTS: I control the setting up and the creation of new accounts within the general ledger system, so that if somebody wants to open a new expenditure account it will come to me, my department, and we will make that decision as to whether or not, first off, it's required, because we may already be able to be accommodate it in a fashion that we already have. And if it is to be created we will determine the specs on where it should be, because every time a new account is created it may impact on your reporting as well. So we're trying to centralize the changes to the system so that the full ramifications can be seen of what that impact would be.

COMMISSIONER POWELL: One of the schedules that Mr. Kennedy had up, in professional fees he talked about software for fixed assets?

MR. ROBERTS: Yes.

COMMISSIONER POWELL: Is that integrated now with the JD Edwards system?

MR. ROBERTS: JD Edwards has a fixed asset module that we are using which is fully integrated with the general ledger, but it is exactly that, it's not a modelling tool.

COMMISSIONER POWELL: Okay.

MR. ROBERTS: So at this point it's not able to do projections using five year plans or 20 years horizons. It can calculate actuals with no difficulty and it can give you your depreciation on actual assets over 20 years, or 50 years, or whatever you require. The difficulty is is that the system was designed as a financial system, not a future modelling system and using what ifs.

COMMISSIONER POWELL: Can you transfer data from the JD Edwards to this software that we saw?

MR. ROBERTS: Yes, and we refer to it as (inaudible) and an S base. This is a modelling system, and what we actually have to do is we take the actual live fixed assets out of JD Edwards and transfer it to this system, and in there then we will input the capital budget proposals, as presented, and do the calculation of future depreciation in that model.

COMMISSIONER POWELL: There is also $65,000 spent on succession software. Does that sort of tie in with your payroll department?

MR. ROBERTS: That is part of the human resources on succession planning.

COMMISSIONER POWELL: But can the data be ... are they tied in or is this a case of they've got to down and do everything again?

MR. ROBERTS: I don't believe it's having to duplicate it. It's an add on feature that supplements what's in JD Edwards.

COMMISSIONER POWELL: Okay, so were these two pieces of software bought in conjunction with the JD Edwards or are these independent?

MR. ROBERTS: They are independent.

COMMISSIONER POWELL: Okay, so when you do up your budgets and you have, I think, 150 business units, they're all controlled through the JD Edwards system?

MR. ROBERTS: Yes. The setting up of the JD Edwards is they use what they refer to as ledger types.

COMMISSIONER POWELL: Uh hum.

MR. ROBERTS: So you will use the same code structure that you use for your actual expenditures.

COMMISSIONER POWELL: Yes.

MR. ROBERTS: So in our actual cost it will refer to ledger type AA representing actuals. When we create a budget we'll call it BA, representing budget. When we move from budget to a forecast it's referred to as BF, so that in the actual recording of the budgets the information that's available for a business unit manager, the account codes are there, he enters on a specific screen the monthly information and there is a text file that's linked directly to that screen for him to add additional text describing what's happening. Once that is in the system that information is available for an inquiry basis to just about anybody in the organization who has the ability to inquire. We restrict the ability of people to enter data for purposes of the budget and restrict it to basically key people in these business unit areas. And once they enter the data we remove their security because it is a true online and an integrated system, and if somebody goes in and either accidentally or does anything else, it's changed automatically.

COMMISSIONER POWELL: Okay. That was my next question. Because you did mention in testimony that department heads and business units, they're responsible to control their own expenditures and their budgets. Okay, I can see, I can visualize now what happens. One of the reasons why we were delayed getting the application was that they ran into some problems entering data on the fixed assets and things. Can you give me just a brief overview what those problems were?

MR. ROBERTS: Part of the problem is, is that you're dealing in calculating items. We're dealing with approximately 35,000 individual fixed asset records, and to move those records and ensure that they're balanced and the calculations are doing the correct calculations in that model is what takes a fair amount of time. In addition to that, you also have anywhere from 150 to 200 capital budget proposals for any particular year, and then you also have the subsequent years, so that, for instance, when we were looking at filing this application we needed the 2000 actuals, which really takes us to about mid February to obtain because you're trying to get your year end audit done and a sign off by external auditors that everybody is happy with these particular numbers. So that information had to be migrated over into the new system and make sure that it balances, because, once again, you're relying on a computer program to move this data and you want to ensure that the checks and balances are entered to make sure that the same data did actually arrive and it provided the results, so that process had to happen. In addition to that, once that was done, then we had to go through the process of entering all the 2001 capital budget proposals, because at that point we were still in a proposal stage because you're talking early in January. They had to be entered and balanced, and in doing that you were really creating almost the same as a fixed asset, so you had to enter the proposal, put a method of depreciation on it and a service life and an end service date, so that had to be done for the year 2001. Then you had to duplicate the exercise and enter all of the 150 or 200 proposals for 2002 and do exactly the same thing. Once that data was in there and it was balanced and it was reviewed to make sure that you were using the right service life, end service date, etcetera, then you would get the model to recalculate depreciation, and the model would then calculate the depreciation based on the actual assets that came over from JD Edwards and it would then calculate the depreciation on the 2001 proposals and the 2002 proposals and put them together. You would also then, of course, arrive at, you know, your total numbers that you would require for your financial statements. So it's purely a function of, I guess, trying to get your actuals resolved at year end because it's always a tedious job trying to get all your accruals done and everything recorded and reviews done, and then it's purely a function of time and resources in which to do it.

COMMISSIONER POWELL: But you wouldn't have the magnitude of problem in your application at 2004 ... 2003, because the ...

MR. ROBERTS: Depending on how the application is done. At this point the volume of work, we will still have to copy over whatever the actuals happen to be at a point in time and we'll still have to deal with the proposals. So for instance, if we're coming back in 2003 for 2004, all the 2004 proposals for the test year will still have to be ...

COMMISSIONER POWELL: No, but all the data on your fixed assets are in the system now. You still got to do the modelling on various things, yes.

MR. ROBERTS: We still got to do the modelling.

COMMISSIONER POWELL: Yes, but it won't be quite as difficult.

MR. ROBERTS: You would have more actuals added to it. Instead of 35,000 records it now may be up to 36,000 or whatever the number happens to be, and what we are trying to do is to deal with the proposals from the point of view of updating them so that we will, hopefully, be able to save in the long run.

COMMISSIONER POWELL: During testimony it was brought up that Abitibi, one of your large industrial customers, have a JD Edwards system. Have you or any of your staff had any contact with any of their staff on looking at problems that they may have had or quirks about the system to sort of sometimes get around Murphy or ...

MR. ROBERTS: There have been some discussions with Abitibi, and I think also Wabush Mines and Labrador also had JD Edwards. The bulk of those discussions had been centred around the maintenance module rather than, I think, on the financial ones.

COMMISSIONER POWELL: In **NP-116**, page 2 of 2, that's a capital budget item. You're talking about replacing your computer systems and going ... and one of the reasons given that in 2002 Hydro will be initiating a One World pilot in order to assess the technology and business implications and moving to One World, and I'm led to believe that One World is just an update of the JD Edwards ...

MR. ROBERTS: It is the ...

COMMISSIONER POWELL: A replacement of?

MR. ROBERTS: It will replace the existing World software that we're ... World Vision software that we're using now.

COMMISSIONER POWELL: Is that the name for the JD Edwards?

MR. ROBERTS: Well, that's the name of the software. JD Edwards is the name of the manufacturer and supplier, but they refer to them like World Vision and then One World.

COMMISSIONER POWELL: Okay.

MR. ROBERTS: So the One World software is an updated version of their software and using a lot more of the current tools like you would see in other pieces of software and using the ability to use web based client server technology.

COMMISSIONER POWELL: You look at this, used the word "pilot" and that's what threw me. It sort of implies that we're going to have a look at it, it might work out, we might want to go to plan B.

MR. ROBERTS: The reason why we're saying a pilot is because of the fact that we'll want to determine the extent and the effort that it will take to do the movement of a product, and we have also been assured by JD Edwards that we can coexist, in other words. We can run both systems because we're not going, as I refer to it, with the big bang of moving everything as we did in the past. We will gradually migrate the modules over to One World Vision.

(12:15)

COMMISSIONER POWELL: But it's my understanding from some of the evidence, that the present system support is going to die sometime in 2005. Could you operate, I mean, if you decided not to go to One World, could you maintain your software yourself with your own inhouse support?

MR. ROBERTS: We'd be able to maintain, I don't think we would. I don't think we have that in depth knowledge of that particular software.

COMMISSIONER POWELL: So you basically have to do something between now and 2005?

MR. ROBERTS: We will have to move to the One World, and one of the things we'll want to do is to take our time and take a particular module, determine the extent and what it does, and look at the time ...

COMMISSIONER POWELL: So the pilot is not to determine if you will move to them, it's just how you're going to move to them?

MR. ROBERTS: How we're going to move and what are the ramifications of moving and how it will eventually fit together.

COMMISSIONER POWELL: So the new hardware, the $2 million that you're saying that you need for new computers, is that just because you're going to need that capacity, because you're going to be operating two fairly large pieces of software at the same time and then you have a capacity problem?

MR. ROBERTS: Well, the existing lease on both of those AS 400s is coming up for renewal. It's not coming up for renewal, it expires in, I believe it is 2002. I'm just trying to get my dates straight now, so we have that issue to deal with, anyway. In addition, we've had JD Edwards now up and running since ... in various forms since 1998. There is other software that we've added to the system but it is non JD Edwards related. We've expanded the availability of this information to all of our various locations, and of course, it is having an impact on the capacity, as well. Historically, prior to this system information could only be provided in a paper copy form. Now there is online access to individual accounts, as well as various reports, all of which both require additional time and effort in that particular area.

COMMISSIONER POWELL: Also in the Section D he talks about the increased capacity, he talks about allowing Hydro to provide a web base for client server interface to computer application. Is this significant in terms of cost of the new software, what you have?

MR. ROBERTS: I can't answer. That's getting outside of an area that I don't really have much responsibility for, except from the point of view of providing my opinion as to what we require.

COMMISSIONER POWELL: So who gives the ... who will give the decision on the cost effectiveness of the software in terms of the additional cost?

MR. ROBERTS: The IS & T department would put together a proposal for presentation to an IT government's committee relative to this and then that would flow through to the management committee.

COMMISSIONER POWELL: So we're looking at somewhere, the capital budget is $500,000 some odd for software, so I would presume that would be the ... so Mr. Osmond probably could give me some more updates on those numbers?

MR. ROBERTS: If you so desire he can do that for you.

COMMISSIONER POWELL: Yeah. One of the other questions ... we got this lovely piece of software now giving all the data and we got these numbers and we got all these cost centres. Then these numbers, I know it's not your responsibility, but it's the same numbers, it's just rearranged in a different way. They're used to produce the cost of service study. Is there any layer in the JD Edwards system that would produce that automatically or is all this data exported out to another piece of software to do the cost of service model?

MR. ROBERTS: The cost of service model is just that, is a separate model. What it does do is there is a program written which will extract this information out of JD Edwards into that particular model.

COMMISSIONER POWELL: Okay.

MR. ROBERTS: And it will take actual, of course, to do an actual cost of service. It will also take the budget or the forecast or whatever we have created.

COMMISSIONER POWELL: Yeah, so who puts the bell on the cat to make sure the same ... I mean, your department is responsible for the primary data, all the costs that goes through the system. When this gets exported what's the mechanism in place to guarantee that that department are using the same live numbers and the same allocations? They're just ...

MR. ROBERTS: There is a balancing routine between the staff and rates that run the cost of service and my staff to ensure that the same numbers are being used.

COMMISSIONER POWELL: Okay.

MR. ROBERTS: And you can actually, if I may, you can actually take some of the information, even in this hearing, and balance that off to what's in my revenue requirement.

COMMISSIONER POWELL: So when we get in doing a cost of service study we should be able to do some correlation back to your revenue requirement cost and breakdowns that you provided?

MR. ROBERTS: It may be very limited and maybe one page or two pages. After that then you start getting the various methodologies in the cost of service allocating these costs based on function and classification.

COMMISSIONER POWELL: Yes.

MR. ROBERTS: So you can at a point in time see that the total cost of my revenue requirement is into the cost of service, and I think that's normally in the first one or two pages of the cost of service. You can literally trace the numbers through it, because I have done it.

COMMISSIONER POWELL: No, I'm just thinking you get transmission, there'll be come down to the point, I'm sure, in the cost of service, whether that should be allocated to an industrial customer as it versus the Newfoundland Power, and got to make sure the total amount that you're dealing with is the total amount and the allocation is the cost of service (inaudible).

MR. ROBERTS: You will be able to trace the total cost on an expense category into the cost of service. Then after that it starts getting into the functionalization and the allocation of these costs.

COMMISSIONER POWELL: Yes.

MR. ROBERTS: And the methodology that's in the cost of service to take pieces of these expenditures and put to transmission or to distribution or ...

COMMISSIONER POWELL: My concern was to make sure that we're still dealing with the same cost. You assured me of that, that shouldn't be a problem.

MR. ROBERTS: Yes, we are.

COMMISSIONER POWELL: Just a small point. When you were talking the other day with, I think it was Mrs. Butler of Newfoundland Power, and there was movement of items from operating being capitalized, and the comment was that if there was extra cost that went into the operating expense but they proved to be capitalized and they were taken out in the bottom end, and you made the comment that wouldn't have any effect on the revenue requirements, because being at the top, at the bottom. But that's not necessarily 100 percent correct, is it?

MR. ROBERTS: In the case of overtime it is correct. If we paid an individual $20, the cost there, that's the $20 that would flow through.

COMMISSIONER POWELL: Yes, but once the cost gets identified as capital, it comes out the end, but then that would affect the depreciation charges at the top because it increases capital, would it not?

MR. ROBERTS: No. Because within the capital budget proposal there has been budgeted by the expenditures in there. It didn't differentiate between salaries or overtime or other related costs. It said here is an estimate of the labour costs that would be associated with it. It doesn't necessarily mean that it's going to change the total cost of the project.

COMMISSIONER POWELL: No, but if you got $1 million in operating costs that you get capitalized, it reduces your direct operating costs, but then when you do your model of depreciation then you have to increase that?

MR. ROBERTS: If these are costs that are charged through to a work order and were budgeted, yes, eventually these allocations of some of those non-construction departments form part of fixed assets which will form part of capital and depreciation.

COMMISSIONER POWELL: I just wanted to make sure I understood the process a bit. Another item that came up was the amortization of the cost of the hearing and the application recommending that that be spread over the year 2002, 2003, but one of the other issues that has been talked about quite a bit since we started was the efforts to get Hydro treated more as an investor owned utility, and there's been a lot of discussions on that, so when I looked at your, I think, interest coverage method of returning revenue for the loss a number of years, and you look at, I think ...

MR. ROBERTS: **NP-2**?

COMMISSIONER POWELL: Yeah, when you looked at that and the base set in G was 1.08, but except for one year Hydro has always been able to achieve that and exceed it. If an investor owned utility was before the Board and they were given targets and ranges within targets, if they were to exceed that they would be required to rebate that back to their customers, so my question to you is why should we look at allowing you to defer costs from one year to another year, when even if it had to be included, that it still would put you over your margin requirements? I mean, that would seem to me not treating you like an investor owned utility where if the emphasis is on treat you like an investor owned utility?

MR. ROBERTS: I guess I just add some general comments for you in that respect. When you look at this regulated coverage and what was created in 1992 the coverage was set towards our utility customers only. The Board didn't set what we could earn on our industrial customers, as an example. It only created what it could do for Newfoundland Power. Hydro was still free to earn a different margin on its industrial customers. It also had, back in 1992, IOC, which is also impacting on these particular numbers. To move forward, the Board does have the right, we've asked for approval to defer these costs. It is the change in legislation that's now requiring us to be fully rate regulated, and circumstances will now change on a go forward basis dealing with what may have been done in the past versus what will come forward in towards the future. The $2 million request to defer those costs in 2001, as I mentioned, until you do the analysis we may still be below 108, but there is no cap established to say that we have to refund or to do anything with earnings in excess of 108. It was a target designed and placed there, but it wasn't to deal with, as I say, putting a cap on it. It was just targeted to aim. As a matter of fact, if memory services me correctly, there were certain things done that are in ... like, as an example, reduce the price of fuel, because I think we had something higher than $12.50 in the rates, and it was a rule of thumb that $1 million, you know, $1 in a barrel and we were burning roughly 3 million barrels of oil would change by X number of dollars, but it was designed back in, from my memory, and participating in that hearing, that it was lead to believe that we could achieve 108 based on the changes that the Board had recommended that we implement, but they never set a cap.

COMMISSIONER POWELL: Mr. Chair, I got one other subject but it's going to take longer than a couple of minutes. You may want to have lunch and get that after.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Commissioner Powell. Thank you, Mr. Roberts. It sounds like a discussion among two people who know their subject matter around accounting quite a bit. I'll have to rely on the transcript a little bit more closely, I think, on some of that discussion. Yes, Mr. Alteen.

MR. ALTEEN: Mr. Chairman, for this afternoon is ... are we to take it that the Board will be an hour or an hour and a half or a half hour? I'm worried more about Mr. Osmond is the only thing.

MR. NOSEWORTHY, CHAIRMAN: I was just going to address that matter, actually. I think from my pole of the Board, the Board will be very quick following Commissioner Powell's line of questioning on his next subject matter. I think we have few questions between us, so quite likely, depending on then the questions arising we could indeed be concluded with Mr. Roberts earlier on in the afternoon. I will advise that the panel would like to conclude at 3:45 this afternoon as opposed to 4:00, and beyond that I'll just have to rely on Ms. Greene to indicate whether she would wish to bring Mr. Osmond forward?

MS. GREENE, Q.C.: Thank you, Mr. Chair. We would like to start with Mr. Osmond as long as it's a reasonable period of time, because Mr. Osmond will be continuing on Monday so we won't have a break in a period of time other than the weekend, so as long as it's a reasonable period of time, say 2:30, 3:00, yes. I don't see the point putting him on if it's 3:30 and we have to break 3:45, but we're prepared to start, depending on the time available.

MR. NOSEWORTHY, CHAIRMAN: Okay.

MR. ALTEEN: We can be ready in all events. We had intended to start with the RSP, and there's ... to bring Mr. Osmond through that. That would probably be best deferred to Monday morning, given the length of it. While we've attempted to make it simple it's never that simple.

COMMISSIONER SAUNDERS: It's a subject for early in the week?

MR. ALTEEN: I would have thought so, so we'll have enough short snappers to take us to the conclusion of this afternoon.

MR. NOSEWORTHY, CHAIRMAN: Okay, and I guess based, again, on questions arising, we'll just have to see where we are.

MR. ALTEEN: That's fine, Mr. Chairman. I was just trying to assess.

MR. NOSEWORTHY, CHAIRMAN: Thank you. We'll reconvene at 2:00.

(break)

(2:00 p.m.)

MR. NOSEWORTHY, CHAIRMAN: Thank you. Good afternoon, are there any preliminary matters before we begin?

MR. KENNEDY: I don't think so, Chair. I'm presuming that undertakings were taken care of earlier, so ...

MR. NOSEWORTHY, CHAIRMAN: Thank you very much, well we'll proceed with Commissioner Powell's questioning of Mr. Roberts, please.

COMMISSIONER POWELL: Thank you. Good afternoon.

MR. ROBERTS: Good afternoon.

COMMISSIONER POWELL: There's only one other area that I want to get at and it's on depreciation since your responsible for that. Just a couple of things from this morning that I just want to get your views on. You may not be able to answer it but when we were talking about the new accounting system, you had mentioned that prior to the JD Edwards, that Newfoundland Power did the billing for your retail customers?

MR. ROBERTS: Yes, Newfoundland Power had a customer billing system that I think was originally their own and which they progressed to and developed a more enhanced, and a completely different version, but they maintained that old one for us and we ran the billings for our rural customers on that old system.

COMMISSIONER POWELL: Okay.

MR. ROBERTS: And the system was never enhanced to the level of being able to provide the features that Newfoundland Power have in its system or what we now have in our new system.

COMMISSIONER POWELL: So was there any exploration of developing their new system to handle your existing retail customers or ...

MR. ROBERTS: I think back some time when we were looking at switching the suite of products that we had, which consisted of various types of products, one of the areas that we were trying to gain some integration with was the accounts receivable package for the customer billings because JD Edwards actually has two accounts receivable. One just deals with the normal type things, and then this one is dealing with what's called the utility customer information system, but they have that type of a system also available for water and gas, so we were able to avail of what they were developing in the utility side which will integrate completely with our system, with what we had acquired.

COMMISSIONER POWELL: From a cost benefit point of view, was there any significant difference in cost with your fellows doing it inhouse as opposed to what Newfoundland Power was charging you?

MR. ROBERTS: At the time that the decision was made to change?

COMMISSIONER POWELL: Well, right now you have a certain cost factor to be able to perform those billings and the process, as opposed to what you were paying Newfoundland Power prior to this.

MR. ROBERTS: I'm just trying to recollect in my memory, going back in time when Hydro was looking at doing something with this particular system. There were discussions with Newfoundland Power as to what could or could not be provided and I'm trying to go from memory. There may have been some cost developed during a proposal maybe from Newfoundland Power versus what it would cost to go on our own, and where we would go from there. This is back in maybe '96 or '97.

COMMISSIONER POWELL: So you don't know off the top of your head right now whether it costed you more to service a customer from an administration point of view than it did prior to the switch over?

MR. ROBERTS: I can't answer that one for you.

COMMISSIONER POWELL: Another item that came up, Legal Counsel had made a comment to you in relationship to your billing with Newfoundland Power, and he made the comment, I think it was why don't you bill more often, and you had said that it wasn't that simple, it was a fairly complex detailed process to do it. The thought that crossed my mind was rather than bill more often, why not bill less but have an arrangement with Newfoundland Power, similar to what Newfoundland Power has with their customers, have an equal payment plan and do an annual adjustment, because when you look at the total revenue billed on an annualized basis to Newfoundland Power, it hasn't changed dramatically over the last number of years, so it would seem like you would save more time internally.

MR. ROBERTS: It hasn't been explored. I guess one of the things that does come to mind is that in equal billing there is an interest cost.

COMMISSIONER POWELL: But this would all work itself through the system, if you were getting, if they were paying you on a weekly basis, say as opposed to a monthly basis, the numbers get crunched through anyway, and whatever the interest cost is there, and what you save on one will offset the other.

MR. ROBERTS: Undoubtedly our interest cost is different than Newfoundland Power's, so there's going to be somebody that's not going to be (inaudible) the same.

COMMISSIONER POWELL: Yeah, okay, without getting into the discussion, their your largest customer, and what costs you more, they're going to pay and what you save, they're going to get the benefit of it in theory anyway, so it's just a comment, something maybe you should look at. The other area I wanted to get into, you're responsible, you said once in your evidence, (inaudible) recent depreciation study and the implication of it in this application. That's what your evidence is going to cover, so I had some notes, since depreciation, I think, is the fourth largest item on your revenue requirement, and unless I missed it, I haven't heard too many people comment on it, but it seems to be there's some significant changes. Page 11 of your evidence ... and I'm just going to do this in the way I had notes when I was reading your evidence, and hopefully we'll cover all the issues. This is talking about two ways of, about salvage costs of assets, but line 13, it says, and it's the last part of it, to estimate net salvage cost in inflated terms ... what does inflated mean there? I know what inflation is, but what ...

MR. ROBERTS: I think it's inflating the actual cost if you were able to determine what the decommissioning costs are and how using a rate of inflation to project out to what it would be in the future at the time of the decommission.

COMMISSIONER POWELL: What kind of a rate would you use? I mean what ...

MR. ROBERTS: Hydro uses an inflation factor in various calculations now, and I'm not sure who is the provider of it, did it come from our economic analysis department, so that would provide us with an inflation factor based on, I think, CPI or something like that.

COMMISSIONER POWELL: So that could be a floating rate in terms of ...

MR. ROBERTS: Just speaking from memory of what I've seen in the last couple of weeks on an inflation factor for another purpose, in the coming five years, I think the rate varies from 1.6 percent up to about 1.8 percent.

COMMISSIONER POWELL: So that factor that was used to increase the cost of an asset, would that be included within the cost of capital assets, or would that be shown as a separate schedule when you do ...

MR. ROBERTS: No, the use of the inflation factor is projecting what the salvage costs are going to be out into the future, if I'm reading from the same item that you are or ...

COMMISSIONER POWELL: But it says if properly calculated there will be a surplus in accumulated depreciation by the end of the asset's life that is equal to the estimated net.

MR. ROBERTS: Pardon me, what is being recommended here by the consultant, that if you know that this is going to happen, you will alter the depreciation rate up so that it will tie in, so at the end of the period the costs are taken care of, as they mention there on line 9, the (inaudible) percentage mark-up calculated based on (inaudible) estimates, so that at the end of the life of the asset, there would be sufficient funds in there then accumulated to account for the salvage.

COMMISSIONER POWELL: So you're talking about inflating the percentage. If you were using one percent, it would be 1.2.

MR. ROBERTS: If it was 10 percent, maybe it's up to 11.6, if that's sufficient enough to take care of the periods that were involved.

COMMISSIONER POWELL: Okay, page 12, line 1, the 1998 study also recommended that an engineering condition survey be conducted for those thermal generating plants that are approaching the end of their presently estimated service lives, so they recommended that ... what was the intention of this recommendation?

MR. ROBERTS: The purpose behind it is that the assets were ... excuse me ... nearing the end of their original established service lives and the study was done to determine whether or not their life would be extended, and if so, to what period of time, so the result of the study and what it looked at was the units at Holyrood and the gas turbines, and based on that study that was done by our internal engineering staff, their recommendations were that these units would be able to sustain at least an additional 20 years, so what we would do is, if the Board approves this recommendation, effective January the 1st, 2002, we will extend the service life of the gas turbines and Unit No. 3 at Holyrood.

COMMISSIONER POWELL: This study was done by Keat Peats, I think?

MR. ROBERTS: KPMG did the depreciation policy study.

COMMISSIONER POWELL: Yes.

MR. ROBERTS: I shouldn't say the depreciation policy ... the depreciation study, and one of their recommendations and one of the issues that we had discussed with them in preparing for this depreciation report, was what do we do with the assets that are getting close to the end of their service life.

COMMISSIONER POWELL: They employed Akers International to do their engineering for them?

MR. ROBERTS: They employed Akers in doing the original assessment of their depreciation report.

COMMISSIONER POWELL: But I noticed when they, the recommendation, the engineering condition survey, that was done internally.

MR. ROBERTS: Yes, it was.

COMMISSIONER POWELL: Any reason why internally as opposed to getting an outside independent view?

MR. ROBERTS: Yes, one of the factors in reviewing this recommendation was that we felt we had the engineering expertise and talent inhouse versus going outside and probably spending another $100,000 or $150,000 to give us the same answer that we felt our own engineering staff could provide.

COMMISSIONER POWELL: So it was the cost.

MR. ROBERTS: It was looking at a cost of could we do the work ourselves and with our own level of expertise, and we felt we did have that expertise and that experience with the items that were being addressed.

COMMISSIONER POWELL: So those inhouse costs, are they shown anywhere, or are they just buried in ...

MR. ROBERTS: They're ... the engineer, Mr. Mallam, which was the lead engineer on the condition survey, is an engineer in the TRO engineering section, and he's a permanent employee of Hydro and he was the lead engineer. The other engineers were also permanent employees, were senior engineers who had actually worked on the construction of the some of these facilities, and of course undoubtedly over time they had been in capital work orders for additional changes that had to be made to those facilities, so we availed of all of that talent and experience in deciding that we would do the engineering condition survey inhouse.

COMMISSIONER POWELL: So there was no budgeted or costed items on this.

MR. ROBERTS: No, we had a ball park number, if I remember correctly, as to what, I think KPMG or Akers had said that it could possibly run us, depending on the level of the study that you wanted to complete.

COMMISSIONER POWELL: I'll just check my notes here to see where ... you make reference there on page 25, I think ... (inaudible) but you only have 13 pages in your report, so that can't be right.

MR. ROBERTS: There's another 14 pages of schedules that are attached. I don't know if it was in one of the schedules.

(2:15 p.m.)

COMMISSIONER POWELL: Oh no, I've got the wrong ... yeah, page 11, it's page 11, line 25. You said the recommendations related to the accounting for the net salvage value of utility assets will be implemented effective January 1, 2002, if approved by the Board. Is that the PUB Board or the Hydro board?

MR. ROBERTS: No, it's the Public Utilities Board.

COMMISSIONER POWELL: So the copy of that, those recommendations and the study has been filed with the Board?

MR. ROBERTS: Yes, it is. I believe they've been provided underneath NP-55. Yes, it's NP-55.

COMMISSIONER POWELL: That's all my questions, Mr. Chairman.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Commissioner Powell. Mr. Saunders please?

COMMISSIONER SAUNDERS: Thank you, Mr. Chair. Just a couple of housekeeping items, Mr. Roberts, good afternoon.

MR. ROBERTS: Good afternoon.

COMMISSIONER SAUNDERS: In answer to a question by Board's counsel this morning in relation to the billing situation with Newfoundland Power, I think his question, it may have been in more than one part, but I thought one part of the question was has it been considered, that is the more frequent billing, and in your answer, I don't have a note of you making any comment on that aspect of the question, has it been considered between ...

MR. ROBERTS: I don't believe it has been considered.

COMMISSIONER SAUNDERS: Okay, fine, and the other question I had was what's your role in relationship to the preparation and monitoring of the capital budget of Hydro outside of your own responsibility as a unit head?

MR. ROBERTS: I have, extremely rarely would I ever have a capital budget proposal. Within the JD Edwards suite of products that we have acquired, there is a module that's referred to as job costs, and that's where we record all of these capital budgets. In other words, we have proposals at this stage. Once the approval is obtained a project manager raises the most current estimate because recognizing that the proposal may have been done six months ago, and now he's getting ready, he has permission to proceed. He will refine that estimate and forward that capital budget work order for approval. Once that approval is obtained, the original contribution provides my staff, and my staff will then set up in this job cost system that budget that's been approved for that capital work order. As things evolve, that number, there will be a number assigned to it. As costs are incurred, costs will be charged to that so that at any point in time a project manager or one of my staff can look at that particular work order online and see what his actual costs are, what his forecasts are, and what his budget is. So that information is available to anybody that has online inquiry into this JD Edwards system. In addition to that, monthly reports would be provided to the vice-presidents of the capital that's involved in their areas, and we also prepare a monthly financial report that comes out of my particular department, and in that we would provide a summarized version of capital and I think the criteria is all capital projects $10 million and above. There is also a small section in the reports to Hydro's board of directors for their various meetings throughout the year advising them as to the current status of our capital program in total. I think I've covered as much as I can remember for now.

COMMISSIONER SAUNDERS: Yeah, maybe you could step back for a minute.

MR. ROBERTS: Sure.

COMMISSIONER SAUNDERS: What I'm concerned about at this stage is, and I'll go back to some weeks ago when we were talking about this matter, there was some debate with respect to the difference between Hydro's budget estimate and the actual numbers over the past ten years, I think, going back to '91 or 92, and I think the evidence was that there was a variance of somewhere around 15 percent. Do you recall those numbers?

MR. ROBERTS: Yes, it's in, I think, the Grant Thornton report.

COMMISSIONER SAUNDERS: Yes.

MR. ROBERTS: They made reference to it.

COMMISSIONER SAUNDERS: That's right, in the Grant Thornton report.

MR. ROBERTS: Okay.

COMMISSIONER SAUNDERS: My question, I guess, is what kind of testing is done to your knowledge with those original, or with those estimates before they're finalized and become a part of the capital budget document?

MR. ROBERTS: I guess I can only relay what I am aware of. It's my understanding that before the final work order is issued, the project manager that's responsible for that is supposed to review these costs and take into account any additional information that he may have before he submits that capital budget for approval internally to Hydro once the approvals have been granted by the Public Utilities Board. So if he has more current information, then that would be reflected in that particular capital work order when he sends it forward for approval.

COMMISSIONER SAUNDERS: Uh hum.

MR. ROBERTS: And it would also make reference that here is the amount that was approved in the capital budget so if there is a change, an increase or a decrease, that would be noted.

COMMISSIONER SAUNDERS: What's your feeling on the variance that was determined by the Grant Thornton report of 15 percent on average over the past ten years?

MR. ROBERTS: I guess I can qualify it this way. The difficulty is in looking back in the past is that, and as I mentioned earlier in my testimony, is that Hydro was looking at the project in total, not specifically in one year so that if the ... and a fair number of our projects involve going over more than one year.

COMMISSIONER SAUNDERS: Yes.

MR. ROBERTS: So the emphasis is on the project as a total, not so much that, you know, I spent $50 in this year and $100 next year, did I get the project done on time and on budget, and if I happen to not get all the costs incurred in year one, but the work is still going and it's on time and in budget, well the emphasis has been on completion of the project, not so much the cash flow within the year. Unfortunately now, or fortunately, I'm not sure which way I want to paraphrase it right now, it is exactly that because the Board is only approving the annual expenditures within the year. I don't think you're approving a project.

COMMISSIONER SAUNDERS: Okay.

MR. ROBERTS: So it's caused some adjustment for people to look at not only the total project but now there's an emphasis on when it's happening within a project as well.

COMMISSIONER SAUNDERS: Thank you, Mr. Roberts, Mr. Chair.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Commissioner Saunders. Commissioner Whalen please?

COMMISSIONER WHALEN: Yes, thank you. Good afternoon, Mr. Roberts.

MR. ROBERTS: Good afternoon.

COMMISSIONER WHALEN: I just have a couple of questions. One follow-up question from Commissioner Powell's discussion with you on the JD Edwards system. Is that system also used for CF(L)Co. reporting and accounts receivable/payable?

MR. ROBERTS: Yes.

COMMISSIONER WHALEN: It is, so all of the work that you do in your role as Controller for CF(L)Co, is also run through the JD Edwards system?

MR. ROBERTS: Yes, within the JD Edwards system, the only difference between the account codes of Hydro and CF(L)Co. would be the first digit to identify the company.

COMMISSIONER WHALEN: Okay.

MR. ROBERTS: Other than that it's basically transparent. They use the same job cost system, they use the same fixed assets, they use the same maintenance, so everything is identical to both companies.

COMMISSIONER WHALEN: Okay.

MR. ROBERTS: There may be some unique accounts for Churchill Falls that would be applicable to Hydro but from an expenditure perspective, salaries is salaries, and everything just happens.

COMMISSIONER WHALEN: In respect then of the capital budget purchases for hardware and software relating to the JD Edwards system, do any of those capital costs get allocated back to CF(L)Co.?

MR. ROBERTS: When the work order was initially raised for the implementation and acquisition of the JD Edwards system back in '97 or '98, CF(L)Co. has made a capital contribution towards that, I think of approximately somewhere between two and two and a half million dollars.

COMMISSIONER WHALEN: Okay.

MR. ROBERTS: And it was based on a ratio developed at that time, so they have made a capital contribution towards the cost of that project, and Hydro has the net cost in its fixed assets.

COMMISSIONER WHALEN: So their capital contribution was up front.

MR. ROBERTS: Yes, well they're paying for it over time to us, but the amount was set up front when the project was first raised.

COMMISSIONER WHALEN: Okay, so ...

MR. ROBERTS: They're paying us over a five year period.

COMMISSIONER WHALEN: The upgrades that you're contemplating now, the new One World, Two World, One, or whatever the new one is, are they going to be ...

MR. ROBERTS: They will have to share in the cost of that as well.

COMMISSIONER WHALEN: Okay, okay, that was, I guess, the ultimate aim of my question. I just have one other question, and it deals with the rate base.

MR. ROBERTS: Yes.

COMMISSIONER WHALEN: And I understand you're responsible for presenting the calculation for the rate base but I have a question really just on the rate base calculation. I think the rate base that you've got in your filing is somewhere in the order of $1.38 billion. I'm looking at your Schedule 2, the average rate base for 2002. Actually it's 1.37.

MR. ROBERTS: Yes, that's the original filing, that's now been revised to $1,367,000.

COMMISSIONER WHALEN: 367, yeah, 557, right?

MR. ROBERTS: Yes.

COMMISSIONER WHALEN: And I'm just looking at the, well the capital assets in particular comprise the largest, the majority of that, but my question really is dealing with, with that rate base in terms of the how the Board is able to deal with the components of the rate base and in particular, I guess, the assets that were put in there and are still in there from way way back, and how the Board can assure itself that all of the components or assets that are in that rate base are actually used and useful from the point of view of our legislation, I guess.

MR. ROBERTS: I think there's two things. There has to be some reliance on the company, and I think the additional check that the Board does have is the use of Grant Thornton in conducting an annual audit, whose test can certainly be expanded to review the additions. I guess the other thing too is that annually now the capital budget is being approved by the Public Utilities Board, and they are the only assets that are going into that capital asset number forming the largest portion of rate base, so there is an opportunity for the Board to question at that point whether or not this is a, quote, "regulated or non-regulated asset" to be included into rate base.

COMMISSIONER WHALEN: I guess though the Board has only really been doing that since 1996, so in terms of the capital budget.

MR. ROBERTS: Yes.

COMMISSIONER WHALEN: The capital budget items, so our oversight there, I think is, I'm comfortable with that. Has there been any independent valuation of the rate base for Hydro?

MR. ROBERTS: No.

COMMISSIONER WHALEN: And my only other question was trying to understand the role that Foster and Associates would have played in calculation your rate base. I know it's referenced in the report, but what would they have actually ...

MR. ROBERTS: Foster and Associates were the ones, are consultants that were retained both for the cost of service and to provide us assistance in developing the rate base, as questioned evolved, as to how we should treat things, how we should do things. They provided that expertise to us. As an example, like in the inventories, whether or not it was a year end inventory versus a 13 month average, and the reason why it was a 13 month average, so those types of questions and assistance were provided to us by Foster and Associates through Ms. McShane, and they did review the information that we had put together and were consulted in doing some of these aspects.

COMMISSIONER WHALEN: Okay, thank you, that's all I have, Chair. Thank you, Mr. Roberts.

MR. ROBERTS: Thank you.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Commissioner Whalen. Good afternoon, Mr. Roberts.

MR. ROBERTS: Good afternoon.

(2:30 p.m.)

MR. NOSEWORTHY, CHAIRMAN: I appreciated your testimony, sir, over the past couple of days. Thank you very much. As a result of that I think I have to pay $12.00 now to the PUB staff who are working over lunch and in the evening on this particular hearing.

MR. ROBERTS: Well, that happens to be a provision that's in our collective agreement and I don't think it's unique to Hydro. I think a lot of the other utilities have a similar provision that if employees are working beyond they get a meal allowance.

MR. NOSEWORTHY, CHAIRMAN: I'm sure it's not. I just have a couple of questions, Mr. Roberts. One, there's been quite a bit of discussion around capitalized costs, I guess, and I don't wish to belabour those but capitalized costs, I understand there's some point in time they're capitalized against the project, and that project is brought on stream and then they're expensed.

MR. ROBERTS: Yes.

MR. NOSEWORTHY, CHAIRMAN: I think that's generally the procedure, and I think you, in your discussion with Mr. Hutchings yesterday on this point, Mr. Hutchings ... "but from the ratepayers' point of view, obviously we shouldn't be paying for projects until the time that they are required, correct?". "Yes", and this is your response, "And I guess all I'm trying to say is that the impact of the cash flow has a significant impact on that ...", and you go on to say, "And right now with the rate base methodology it's critical to make sure that it is as close as possible to what it should be, both from a ratepayer as well as for the company."

MR. ROBERTS: Yes.

MR. NOSEWORTHY, CHAIRMAN: And I guess my question relates to at what point in time does a project get brought on stream, what's the criteria, how do you make that decision, and how is it handled internally from an accounting point of view?

MR. ROBERTS: Well, the project manager in raising the original capital budget proposals stipulate inservice dates.

MR. NOSEWORTHY, CHAIRMAN: Okay.

MR. ROBERTS: And they would also indicate in that proposal as an example, if they're replacing an asset, which assets they are replacing, so that's a side benefit to my staff in looking at and recording these fixed assets, that we have an indication of the assets that are being replaced, so that we can start to develop is there a loss or a gain on the disposal of these assets coming up, and make a provision for it. As the work order is raised, of course, the time has progressed and hopefully there is a more refinement of current information, if it is available, and that may or may not impact the service date, the inservice date, and I guess what I was trying to say is that within 2002 if those inservice dates change then they're not going to be in or out of rate base, so if we don't get it in rate base on such time as you come back and actually have a hearing and include these assets in rate base, then really you're not recovering costs on those things, they are partly coming out of your profit.

MR. NOSEWORTHY, CHAIRMAN: Understood, yeah, so the inservice dates as you refer to them, that's the date that the asset or the project becomes operational or is available, is used and useful based on ...

MR. ROBERTS: Is supposed to be used and useful, and available for generation of revenue or provision of power.

MR. NOSEWORTHY, CHAIRMAN: So is there a definition of that used and useful?

MR. ROBERTS: We do have a definition of an inservice date, and as I mentioned, I think one is being available to generate power, and I think there are two others that we use as a definition of being in an inservice date.

MR. NOSEWORTHY, CHAIRMAN: So specific criteria.

MR. ROBERTS: Yes.

MR. NOSEWORTHY, CHAIRMAN: I see, okay. Thank you, you had mentioned in relation to a discussion, I think, with counsel this morning, the idea that there is a performance, or an incentive, a management incentive program in place at Hydro. I believe that's correct.

MR. ROBERTS: It's on a pilot basis, it commenced this year.

MR. NOSEWORTHY, CHAIRMAN: I see, and you talked about the, some of the requirements and some of the responsibilities certainly that you have to meet specific targets and objectives, and how are those targets and objectives set for you? Who does that and how are they actually promulgated in that sense?

MR. ROBERTS: Directly to my own department would be between my Vice-President and myself as to these targets that we would establish for the year, and I would agree to those. Then as you move up, I would also be involved on a divisional level that would affect myself as well as the other three managers that report to the Vice-President of Finance, and then the management committee would be dictating the corporate-wide objectives that the senior management would participate in.

MR. NOSEWORTHY, CHAIRMAN: So is it fair to say that Mr. Osmond would set your targets, or would you have input and they would be derived through discussion and would they be based on management objectives that would be set and therefore it would filter down and you would set objectives to your staff as well?

MR. ROBERTS: It would filter down from the top coming down, and then maybe ... it would start at the top and come down as being the corporate objectives to divisional and then to my particular department, and there may be some objectives that I may have which are solely objectives towards my department that may have a very negligible impact on the corporation as a whole.

MR. NOSEWORTHY, CHAIRMAN: Right.

MR. ROBERTS: But it may be important in my particular area, for instance, in assigning of staff and how we can get things organized and done, or accomplished quicker or faster, so the impact up to the corporate level may be very small, but to me and my department it could mean a big gain in how I do things.

MR. NOSEWORTHY, CHAIRMAN: This may be a question best addressed to Mr. Osmond, and I'll certainly do that, but I'm trying to understand other people's, other employees' roles in this as well. You've gone through a strategic planning exercise, so would these objectives and that be set on the basis of an actual business plan and filtered down through the organization?

MR. ROBERTS: The strategic planning process is still ongoing and we're trying to progress and advance that process in between this hearing and as time avails, and recognizing that it's not just the people that are involved in here, but other vice-presidents and senior managers in Hydro, so we are endeavouring to progress them as best as we can.

MR. NOSEWORTHY, CHAIRMAN: So the business planning exercise is really not operationalized if you will within Hydro at this point.

MR. ROBERTS: Not fully implemented and up and running, but the objectives are being tied to where we see the strategic planning going.

MR. NOSEWORTHY, CHAIRMAN: Okay, thank you. The other, I made a note ... in the professional services there was $65,000 for career succession software. What would that be best ... who would respond to that question?

MR. ROBERTS: You will have to put it to Mr. Osmond.

MR. NOSEWORTHY, CHAIRMAN: Okay.

MR. ROBERTS: It falls underneath the responsibility of Ms. Greene, Human Resources and Legal Counsel.

MR. NOSEWORTHY, CHAIRMAN: Okay, I'll put Mr. Osmond on notice for that question. That's fine, Mr. Roberts, thank you very much. That's all the questions I have.

MR. ROBERTS: Thank you.

MR. NOSEWORTHY, CHAIRMAN: We'll proceed now directly to questions on matters arising, and I'll ask Newfoundland Power if they would have any questions please?

MS. BUTLER, Q.C.: Nothing arising, thank you, Mr. Chairman.

MR. NOSEWORTHY, CHAIRMAN: Industrial Customers?

MR. HUTCHINGS: Just one point to clarify, Mr. Chair, Mr. Roberts, both in response to Mr. Kennedy earlier today, and again in response to Commissioner Whalen, in talking about the supplies inventory I was led to believe today that the number that's in the rate base, and it happens to be on the screen in front of us, the $21,095,000, was actually a 13 month rolling average, whereas I understood from our discussion of yesterday that that was simply the December 31 balance. Can you clarify which it actually is?

MR. ROBERTS: The $21,095,000 is a December 31st, 2000 number, and what we did do, is we did look back over the year 2000 and see what that number was in relationship to the 2105, and it was close enough that we just went with that particular number.

MR. HUTCHINGS: Okay, because I was fairly certain that I had heard you say to Mr. Kennedy in answer to a question that ... or actually it was on redirect, that the 13 month average is used in the rate base, but that's not the case?

MR. ROBERTS: Not in the case of the supplies inventory. It's used in the case of the fuel inventory.

MR. HUTCHINGS: Yes, I understood that.

MR. ROBERTS: Where we do actually have a projection of the Bunker C and the diesel fuel.

MR. HUTCHINGS: Okay, thank you. That's the only point I had, Mr. Chair.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr. Hutchings. Mr. Browne, do you have any questions?

MR. BROWNE, Q.C.: Yes, we have a few questions, Mr. Roberts. Commissioner Whalen asked you concerning CF(L)Co. and JD Edwards, and the costing of that. Have you ever had a complaint from Hydro Quebec in reference to any costing Hydro has allocated to CF(L)Co.?

MR. ROBERTS: I'm not aware of any complaint, but maybe I can give you a little bit of history. Back in my time with Hydro, and I started back in '83, and became Controller in '85. In the earlier days the CF(L)Co. administrative fee between CF(L)Co. and Hydro always formed part of the budget. In the latter years the board of directors of CF(L)Co. which would include representatives from Hydro Quebec, wanted to have detailed information provided, and specific approval, and what we have attached in **NP-11(b)** is an exact sample of ... it's not a sample, it is an actuality of what we provide to the CF(L)Co. board of directors for their approval and consent, so they literally agree to what the fee is. The Vice-President of Finance attends those meetings and provides a financial report as well as is prepared to address and answer any questions as to why things are changing and what we have done in that respect, so the amounts are reviewed and then the information is provided and made available to the CF(L)Co. board of directors for their consideration.

MR. BROWNE, Q.C.: So you've had no complaint then from Hydro Quebec.

MR. ROBERTS: Not that I'm aware of.

MR. BROWNE, Q.C.: And that, of course, leads the question, are you sure you're charging enough to CF(L)Co.?

MR. ROBERTS: From my perspective, I think we're being reasonable.

MS. GREENE, Q.C.: We are aware Hydro Quebec pays one third through their share holdings.

MR. BROWNE, Q.C.: This morning you were asked questions concerning the interest which has accumulated in the Rate Stabilization Account over the years. You are aware now, of course, that CA-216, and CA-217 were filed yesterday.

MR. ROBERTS: Yes, I am.

MR. BROWNE, Q.C.: And these two documents give specifics in reference to the interest that's accumulated since the inception of the Rate Stabilization Plan. I don't believe these are available electronically yet, are they, Mr. O'Rielly? Maybe the witness can confirm those figures for us.

MR. ROBERTS: CA-216 provided the year end balances of the Rate Stabilization Plan since 1986, up to and including September 2001, and CA-217 was the interest that's been charged to the Rate Stabilization Plan either by year since I believe 1986, and if I remember the number, I think it's a total of about $15.2 million.

MR. BROWNE, Q.C.: You must have prepared the documents, did you?

MR. ROBERTS: My staff put it together so I have reviewed it, and I do remember the numbers.

MR. BROWNE, Q.C.: Yes, I just wanted to point out that these documents are there and are available. You were asked a number of questions concerning JD Edwards, and I mentioned this to counsel during lunch. Would it be possible, since we've heard so much about JD Edwards, to take a view for counsel and indeed the Board, to take a view to see how JD Edwards operates. Is that possible?

MR. ROBERTS: I believe it can be arranged.

MS. GREENE, Q.C.: We may be able to arrange for it here through this monitoring system, if that's the wish of the Board.

MR. NOSEWORTHY, CHAIRMAN: I'd be interested in that as well, I think, I don't know about my colleagues.

MR. BROWNE, Q.C.: I'm sure, in order to get a break, none of us would be adverse to travelling to Hydro and taking a look and ...

MS. GREENE, Q.C.: You can come to Hydro if ... you're welcome at Hydro Place any time as well.

MR. BROWNE, Q.C.: And see if JD Edwards can make us a coffee and give us a donut too.

MS. GREENE, Q.C.: We provide the coffee but no donuts.

MR. BROWNE, Q.C.: Okay.

MR. NOSEWORTHY, CHAIRMAN: We'll arrange for that.

MS. HENLEY ANDREWS: As long as it's not in the revenue requirement.

MS. GREENE, Q.C.: No, no, everything like that goes in the revenue requirement.

COMMISSIONER POWELL: Don't bring your spouse *(laughter)*.

MS. GREENE, Q.C.: I don't think my spouse would be interested, Mr. Powell.

(2:45 p.m.)

MR. FITZGERALD: Mr. Chair, I just have one question arising. Mr. Roberts, it arises from a question put to you by Commissioner Whalen. It relates to Foster and Associates' assistance to Hydro in preparing the rate base figures.

MR. ROBERTS: Yes.

MR. FITZGERALD: And that's in total, they assisted you line-by-line with this?

MR. ROBERTS: They provided some basic guidance, as I mentioned, like in the case of the inventory, because of the volatility with the fuel, that we should be using a 13 month average, so therefore you wouldn't end up with the highest amount in the rate base. It should be based on the average and you're taking out the situation where the inventory is the highest at the end of December, so it would eliminate that bias, so it was that type of advice that they provided to us, and of course, with that advice we then prepared the necessary information and the numbers. When the numbers were done, of course, they were provided with this information for their review and if they happened to see something that wasn't right or something that seemed strange in their opinion, then they would advise us accordingly.

MR. FITZGERALD: Is there any intention to disclose any of that correspondence with Foster and Associates on this issue at this hearing?

MR. ROBERTS: No, and most of the correspondence would be via the telephone call or photocopying or electronically sending, as an example, this page of the rate base to Foster and Associates, so there wasn't a formal written request for information, it was by phone calls and electronic mail.

MR. FITZGERALD: Would it be difficult to assemble the communication?

MR. ROBERTS: I really don't know because most of the information wasn't done by me, it would have been done by the rates department or staff in my area.

MR. FITZGERALD: That's my questions.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr. Browne, and thank you, Mr. Fitzgerald. Mr. Kennedy, do you have any questions?

MR. KENNEDY: Just one question, Chair. Mr. Roberts, there was some questions concerning, by Commissioner Powell concerning the net salvage costs being added to the accumulated depreciation of your prime assets, and I take it this is, as I understand it correctly, so that on the theory that at the end of the depreciation period the asset is no longer useful and you will have built a provision in for salvaging.

MR. ROBERTS: You will have built up a provision to cover the cost of the salvage at that point in time.

MR. KENNEDY: Now in the case of, for instance, Units No. 1 and 2 at the Holyrood station, the useful life of those assets has been extended a significant number of years beyond what was originally anticipated.

MR. ROBERTS: In the case of units one and two, they were fully depreciated in 2001 so in the case of Units 1 and 2, all we are dealing with is additions to those particular units and we treat it as a piece of equipment because the plant is fully depreciated for Units 1 and 2.

MR. KENNEDY: Sure, what would happen though from an accounting perspective if you had been adding a salvage provision into the depreciation of Units No. 1 and 2, so that now we would actually have a positive balance in the account built in for that salvage, but we're not actually going to salvage, so ...

MR. ROBERTS: If it had to have been done back in time, what you would have now is sitting on the balance sheet a liability to which the future payments could be charged. In reality, if that had to have been done by the depreciation expense going through the revenue requirement, the cost would have been recovered each year the depreciation expense was being recorded, so that the liability already existed and funds had been received so that the payment of those funds then wouldn't impact on the, the payment of those costs would not impact on the current year's operations.

MR. KENNEDY: Okay, that might be one I need to go speak to Mr. Brushett about to see if I can get an interpretation on that. So it's not the case then that by depreciating the asset down faster than as it actually happened to be the case, that you would, your depreciation expense ...

MR. ROBERTS: Well what you would do is you would be using a higher rate, like instead ... as I mentioned, instead of using ten percent, if you had said, well, look, an extra one percent would give me the value of those net salvage costs ten years into the future, so by putting through the 11 percent, then you would accumulate a liability, very similar to the employee future benefits.

MR. KENNEDY: Uh hum.

MR. ROBERTS: But you've got this recognition being done.

MR. KENNEDY: Yeah, and on a straight line that implies that you'd have ten years of useful life for that asset.

MR. ROBERTS: Well, whatever happens to be left on that particular life.

MR. KENNEDY: And then at the end of the ten years you've now got this asset fully depreciated down, plus a provision built for salvage.

MR. ROBERTS: Plus I have the provision up here, that's correct.

MR. KENNEDY: But if the asset actually ended up having a 20 year life span, you now have built up a provision for salvage premature to what you actually require, correct?

MR. ROBERTS: What would have to be done is that if you were to do a revised condition survey, then one of the things that would have to be done would also have to make the review of this as well, so both would have to go on parallel.

MR. KENNEDY: Okay, so from an accounting perspective, that provision for the salvage would get taken care of during the extended life of the asset.

MR. ROBERTS: That's correct, you would revise both.

MR. KENNEDY: That's all the questions I have, thank you, Chair.

MR. NOSEWORTHY, CHAIRMAN: Thank you, Mr. Kennedy. Ms. Greene, any redirect?

MS. GREENE, Q.C.: I have no redirect for Mr. Roberts, but I did have a comment in response to questions by yourself, the Chair, to Mr. Roberts on the incentive plan. I just wanted to point out that U-Hydro No. 12 contains a description of the incentive plan and the corporate objectives that were set at the top and then how it works down to the divisional level, and there is a sample attached to that, so that's U-Hydro No. 12 for the description of the incentive plan and an example of how it works.

MR. NOSEWORTHY, CHAIRMAN: Thank you for that information, Ms. Greene. Is that it?

MS. GREENE, Q.C.: Thank you, yes.

MR. NOSEWORTHY, CHAIRMAN: That concludes Mr. Roberts' testimony?

MS. GREENE, Q.C.: Yes, thank you very much.

MR. NOSEWORTHY, CHAIRMAN: Thank you very much, Mr. Roberts. Your testimony was very direct and clear I thought, thank you.

MR. ROBERTS: Thank you.

MR. NOSEWORTHY, CHAIRMAN: I guess I'd be looking for direction now. We had talked ... I would propose, if we were going to begin with Mr. Osmond that we break and allow Mr. Osmond to get prepared and probably come back at 3:00 *(sic)*. That would give us 45 minutes, but I'm totally at your discretion on that.

MS. GREENE, Q.C.: And I guess Hydro is ...

MR. NOSEWORTHY, CHAIRMAN: I was understanding that if there was 45 minutes or an hour left you'd like to bring Mr. Osmond on and I was understanding that Newfoundland Power would be prepared to begin for that period of time. Is that still the case?

MS. GREENE, Q.C.: I guess we're agreeable whatever the parties wish. Mr. Osmond is ready to start. We recognize we have this break at quarter to three, and I don't know if we would be back by 3:00. I guess that wouldn't be a regular coffee break, would it, because ...

MR. NOSEWORTHY, CHAIRMAN: No, we would like to finish at quarter to four this afternoon promptly.

MS. GREENE, Q.C.: So really whatever is agreeable to the parties. If the Board wishes to start with Mr. Osmond, Mr. Osmond is ready to start. If we determine with the coffee break and leaving by quarter to 4:00 is only a half an hour, it's almost not worthwhile, that is really up to the parties and to the Board.

MR. NOSEWORTHY, CHAIRMAN: I could go around, and I don't see ... personally I don't see the utility to some degree in starting this afternoon with Mr. Osmond.

MS. BUTLER, Q.C.: Mr. Chairman, we're quite flexible really. It's Friday and it's been a long week. I think we've accomplished a lot quite frankly.

MR. NOSEWORTHY, CHAIRMAN: I think so, I think we'll break now until 9:30 on Monday morning at which time Mr. Osmond will take the stand hopefully. He looks ... I'm not sure whether he looks relieved or upset, but anyway, Mr. Osmond, we look forward to seeing you on Monday morning.

(hearing adjourned to November 19, 2001)