October 16, 2003
(9:05 a.m.)
CHAIRMAN:
Q. Good morning. Good morning, Ms. Newman, are there any preliminary matters before we get started, please?
MS. NEWMAN:
Q. No, Chair.
CHAIRMAN:
Q. Thank you. Good morning, Mr. Roberts.
A. Good morning.
Q. Looks like it might be your last day on the stand, I'm sure you're looking forward to that. Good morning, Mr. Seviour.
MR. SEVIOUR:
Q. Good morning, Mr. Chairman.
CHAIRMAN:
Q. You can begin your cross when you're ready, please.
MR. SEVIOUR:
Q. Thank you, Mr. Chairman. Good morning, Mr. Roberts.
A. Good morning.
Q. Mr. Roberts, I wonder if I could ask you to turn up Exhibit JRH-1, this is the Fuel Oil

Practices Review and Policy. I'm assuming that you personally did not prepare this document, this is Mr. Haynes' document?
A. That document was prepared for Mr. Haynes, yes.
Q. Can you tell us, were you involved in consideration of hedging as a potential strategy for Hydro?
A. Hydro hired an outside consultant to provided us with the advice relative to all price hedging.
Q. And, as I understand it, within Hydro, according to your evidence and that of Mr. Haynes, it's the production division that has the responsibility for the management of oil purchases and oil pricing issues, is that correct?
A. Yes. Mr. Haynes, through his division in production has full responsibility for all matters relative to fuel.
Q. Did you yourself have any involvement in assessing the hedging, fuel oil pricing hedging issue for Hydro?
A. I personally did not.
Q. You did not, okay. Are you aware of the

conclusion that was achieved that a fuel oil pricing hedging program would not be a recommended strategy for Hydro?
A. Yes, I have read the document, I'm aware of the conclusions that were reached.
Q. And I don't want to spend much time on this, Mr. Haynes is the person to deal with it, but at page three of the report, if that could be turned up, there is a discussion of one of the reasons why hedging was ruled out as a potential fuel oil pricing strategy management and one of the reasons given was that although there may be an appreciable benefit of ten percent in adding hedging to the RSP strategy to allow a ten percent decrease in price volatility for consumers, the attendant, administration and related costs of such a program probably outweighed that benefit. Are you aware of that conclusion?
A. Yes, I'm reading it here on the screen, as you say, and as I say, I have read the report earlier.
Q. And my interest in coming to this with you is at page three where there's a reference to the potential significant cost on the first line

associated with the management of the hedging program. Were you involved in assessing any of those costs?
A. No, an outside consultant provided assistance to Hydro in the development of that and this information was done through our Treasury Department and the consultant for Mr. Haynes.
Q. I'll come to Mr. Haynes with that, and move on, thank you. I spoke with Mr. Young yesterday and let him know that I would be covering a few technical points with you, Mr. Roberts, on a few issues that I've been directed to explore by the Industrial Customers' experts and I wanted to come to those now.
The first point relates to your evidence
at page 15 of your evidence, Section 4.6. 4. 6
you talk about the cost of debt and perhaps for the record you can just read what your evidence is.
A. Yes, beginning on line 16, "The calculation of the cost of debt is contained on Schedule 7, attached, and is consistent with the
methodology approved by the Board in P.U. 7
during the 2001 GRA. The forecast for 2004 is

MR. ROBERTS:
8.29 percent versus 8.17 in the 2002 test year final cost of service."
Q. And that represents an increase over the 2002 test year cost of service, is that correct?
A. Yes, it does.
Q. Before we look at the numbers that relate to this particular conclusion, can you give us an explanation as to why the cost of debt would be higher for the 2004 test year than it was for the 2002 test year?
A. Well two things that immediately come to mind is the financing cost associated with the completion of the Granite Canal project and the continued build-up in the Rate Stabilization Plan.
Q. I guess intuitively when I looked at that, when I first read your evidence, and as I say, we have some numbers on this that I'll be coming to in a moment, but when I first read your evidence, intuitively, it surprised me that in 2004 when the context of interest rate decreases, we would be seeing an increase in the cost of borrowing, and I'm wondering if you could react to that?

A. But we have more debt outstanding in total and there is a switch between funds being financed on a short-term basis because we were capped at a total of 300 million. And as we approach that 300 million, plans are put in place to convert to a long-term debt issue and a long-term debt issue would carry a higher interest rate than what would be obtained in short-term.
Q. Why don't we just move to the Exhibit I've given notice to you of, that's IC-238. IC-238 is a three-page document, Mr. Roberts, in which you've broken down the cost of debt for both 2002 and 2004, is that correct?
A. Yes, it shows the final cost-of-service debt calculation for 2002 and the proposed forecast cost-of-debt calculation based on the revision in August. No, I'm sorry, it's based on the original filing, I'll correct you there.
Q. Let's turn up page two then of IC-238 and we see that in this Exhibit which relates to 2002 cost of debt, the figure achieved was 8.166 percent. That's in the bottom right hand corner of the document.
A. Yes, that's correct.

Q. And can you just clarify how that particular figure was achieved and take us through in a general way, this Schedule so that we can meaningfully understand how you got to that figure?
A. Yes. Maybe if we can just start at the top of the screen. The first section is headed up as being our Canadian Bond Interest. These are the long-term debt issues that are outstanding, indicating the year of maturity, the balance that was outstanding in 2001 versus 2002, giving you an average. And then the last column over indicates the amount of interest that's associated with that particular debt issue. The sum of all of those is that there's approximately $90,783,000 worth of interest associated with an average of 1.2 billion dollars worth of debt.
The next line shows some other long-term debt which are government of Canada issues, showing the same information as to what's outstanding as of December 2001 and December 2002 to arrive at your average, and the total interest cost on that is 1.7 million dollars.

We have some capital leases that are outstanding and associated with those, there's an average debt outstanding of 3.3 million and the interest cost of 355,000 dollars. Our short-term debt which happens to be the promissory notes that we have, that's a--where our short-term borrowing and as you'll recall, a few minutes ago I mentioned we have a cap of 300 million dollars. That's the area where the short-term promissory notes are recorded. At the end of the period, we have an average outstanding of 195,870,000 and the interest based on a month-by-month calculation of the activity that's happened within the run, for the calculation of the interest, the annual interest cost is $5,952,000. The next line is the amortization of our realized foreign exchange losses on two pieces of debt that were in foreign currency. And the total amortization on those is $2,157,000.
The next section deals with the discount in issue expenses. And just very briefly on that is that when we go to the bond market to issue a 125 million dollars, there are fees for which we have to pay and it's the

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MR. ROBERTS:
amortization of those fees that are matched over the life of the debt. Fiduciary fees are some fees that are handled for the administration of the debt, the same thing associated with the MS lease in moving you down to a line called "Total Interest Expense" of 102,028,000. The guarantee fee on the debt that's outstanding, for which the province has paid a fee of one percent, is 12.7. We've included in, within this section of funding, we also have some debt on our books that's done on a month-by-month basis, relative to our investments, CF(L)CO, that's been financed and the average debt that's been outstanding based on 2001 and 2 is 26 million, 653. The interest cost associated with that has been calculated at $1,891,000, so that comes off of the total interest.

The guarantee fee, of course there's a portion of the guarantee fee associated with the debt on CF(L)CO because all our debt is guaranteed by the province. So the amount in guarantee fee that's associate with the debt related to CF(L)CO is 278,000 and that comes

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off. And then finally, Hydro has some sinking funds relative to these various long-term bond issues. There are statutory requirements where we are required to put aside a certain amount of funds each year to allow for the availability of funds upon retirement of the issue. So the amount of the sinking funds that are directly related to that debt are reflected here and they end up being a reduction off of the total debt that's outstanding, and the interest that's earned on those particular funds is 6 million, 306. And when we sum all of those costs and reductions together, we end up with a total interest bill of a hundred and six, two sixty-six. The average of the debt outstanding between 2001, 2002 is one billion, three hundred one, three eighty-five and that is divided into the total interest cost, you end up with your rate of 8.166 or 8.17 as rounded in my evidence.

Q. You're dividing 106,266,000 by a billion -

A. The 1,301,385 which is the average debt

Q. Thank you, that's helpful, Mr. Roberts. Can I ask you to return to the discount and issues expense and there's a reference just a few

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lines down from that, "Total DDI". DDI, is that the same thing?

A. Yes, discount and issue expense. That discount and issue is what the DDI represents.

Q. Could you amplify a bit on what are the nature of these expenses that are reflected in this category?

A. Well, what would be there is that, for instance, when we go to our financial advisors and say that we're looking at an issue of $125 million, then there is a fee to those bond sellers as I would refer to. So that we don't get a full $125 million, we may get 123 million, five hundred. So there is a fee or a commission, whatever you prefer to refer to it, associated with selling that issue. So we actually sell the issue to that group and they actually go out and would re-sell the bonds to various investment dealers or pension plans, whatever the case may be. So, there would be a fee to the actual financial advisors for selling these bonds and there may be some printing costs or other costs from a legal perspective in finalizing some of the documents.

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Q. And the figure that we see in parentis there, of eleven eight eighty, that's a simple average of year end 2001, year end 2002.

A. Yes, it is.

Q. And it's expressed as a negative here but I take it from my own review of the Math that what you do is in fact you don't deduct it from the -

A. You actually add it on because -

Q. You add it.

A. Yes, because you didn't really get the full face value.

Q. That's right. So it's a cost of debt.

A. Yes.

Q. And so we shouldn't be mislead by the fact that it's shown as a deduction in this Schedule. I think that's helpful, Mr. Roberts. Can I ask you now to turn to page three of three, and I won't ask you to go through the same exercise, but the same approach is used, presumably, in the 2004 calculation of debt to get 8.2832 percent?

A. Yes, that's correct.

Q. I want you to turn to the discount and issues expense that's shown in this schedule which

MR. SEVIOUR:
confused us, because if you look at the debt discount and issues expense reflected on this schedule, it's expressed to be an average of 6,171,000, is that correct?
A. Yes, it is.
Q. And that's shown in this particular schedule as a credit as opposed to a deduction?
A. Yes, that's correct.
Q. That would indicate that there's been something in the nature of an 18 million dollar swing between '02 and '04 test years?
A. Yes, if you would just bear with me for one second, I can explain as to why.
Q. And that's the point of my question, perhaps you can do that.
A. You will notice there's a series there underneath that section, 5.05 percent and you will come across into the column and it shows in brackets, 270 thousand. And then you will also notice there is a 6.65 percent issue there as well that shows in brackets, an amount of 314,000. In our borrowing, of course, 6.65 for 2004 was just a projection, but what had happened, we opened an existing

series for the 5.05 and in opening that issue, the bonds were sold at a premium, so that instead of being sold at $100, people were willing to pay $110, and I'm just using hypothetical numbers. They were willing to pay more than par to be able to obtain a bond with a 5.05 percent interest rate. That excess that we received, we're writing off back against interest expense over the life of the debt issue.
In the preparation of the 2004 forecast and looking at the requirements for another issue, the same thing was done for the filing that we have before us of saying that we would have opened an existing 6.65 percent bond issue. Selling that particular issue, people would have been prepared to pay a premium to get that interest rate. So, therefore, we would have received the same principle if people would be willing to pay more than $100 for the face value of a bond, to obtain an interest rate factor of 6.65. So we ended up factoring in here that we would receive a premium on that issue, and that's why you end up having a credit or a reduction

in your interest expense and the debt discount on issue expenses on those two issues.
In actual fact, as been outlined to date in a hearing and also in one of the RFIs, what has actually happened in reality is that we didn't open an existing issue for the 6.65, there was actually a new issue that was issued at 5.7. So the impact of all of this will be reflected now in the new revision.
Q. And was there still a premium associated with that bond issue?
A. No, there was not.
Q. So this figure will be reduced.
A. This figure will disappear on the revision.
Q. And just, finally, to complete the circle, but in the method of calculation, can you confirm that in attaining the average debt for the purposes of the calculation on page three, that because this was a credit to Hydro based on the premium of the bonds of 6,171,000 as calculated, that that figure actually will be deducted in going through -
A. The premium, because it would actually increase the amount of debt, it goes in reverse of what we talked about earlier.

Q. Thank you. That's helpful, Mr. Roberts. I wanted to turn now to the next issue I raised with Mr. Young, for your review. And that's the differences that are found in the Cost-of-Service Study and in your Schedule 2 respecting the interest and the return on equity computations. Are you aware of this issue?
A. Yes.
Q. And I guess we have Schedule 2 on the screen and let's begin with the interest figure which is in line 34. And that figure is reflected in your calculation to be $101,715,000?
A. Yes.
Q. That's in the shaded portion on line 35?
A. Yes.
Q. And if I could ask that Mr. Greneman's evidence be turned up, this is the Cost-of-Service study. And Mr. O'Reilly, I'm referring to page one of 107. And I'm looking at line 21 of that schedule, a return on debt. That corresponds to the interest cost that we just looked at, does it not?
A. Yes. Maybe I can help to explain -
Q. Maybe we'll just get--do you mind if I ask

MR. SEVIOUR:
just a couple of more questions -
A. No, go right ahead.
Q. - before we get to the explanation.
A. Okay.
Q. So we have the table set somewhat. But this figure of $106,037,664, that's, in fact, higher than your cost of interest that's shown in the revenue requirement that we just looked at, is that correct?
A. Yes.
Q. And just to complete the loop on this, again, so that the Board has a sense of the issues we're going to explore and I'm going to have you attempt to explain to me. If you look at line 22, the return on equity in Mr. Greneman's schedule in front of you is $15,052,375, is that correct?
A. Yes.
Q. And that, in fact, is lower than your Schedule 2 number, and maybe we can flip up Schedule 2 again, Mr. O'Reilly, if you don't mind. And at the bottom of the page where we have the corresponding entry for margin return on equity, line 35, there's a figure of

19,384,000 as opposed to the 15 million and change of Mr. Greneman's, is that correct?
A. Yes, it's higher than what's in Mr. Greneman's.
Q. So we have a variance for the two categories and I just wanted to explore a bit of that with you because there's been some requests for information responses filed on this, and we're having some difficulty in determining exactly how those amounts could be reconciled.
Perhaps we can start with IC-405, and I'm going to come at this, Mr. Roberts, by dealing with the interest expense discrepancy first. And I don't know if you had any general comments to make as to why Mr. Greneman's cost-of-service interest calculation and your own in Schedule 2 for the revenue requirement, would differ, before we got into this particular document.
(9:30 a.m.)
A. Maybe I can try to provide a little bit of an overview first and then come back to the issue at hand of what's on the screen of IC-405. If you look at my revenue requirement which we just referred to on Schedule 2, if you add the

line 34 and 35 together, the interest and the margin, that comes to at least on a revised filing, 121 million, 088. And, I believe, if you went back to Mr. Greneman's cost of service and you added what he shows for interest and margin, you should come to the same number.
Q. As I understand it and I don't want to interrupt you, but both are revenue requirement calculations, are they not?
A. Mr. Greneman's is the cost of service for determining rates. My revenue requirement is reflecting what an Income Statement would look like, even though it's called a revenue requirement. So, what I'm saying is that the total return that Mr. Greneman has used in the cost of service to determine rates is exactly in total the same as I have in requirement, in the revenue requirement.
Q. You've just gotten to that total differently.
A. The split of what is interest versus margin is done differently and I'll come to that now in a second. But I want to be sure in that if you look back into my evidence, the return on rate base that's calculated is the hundred

twenty-one 088, that's what Mr. Greneman uses in the cost of service for setting rates. And what I show is just the allocation from a financial and reporting basis of what that split would be between interest and profit. So there's no difference here, it's just how do you allocate the pot. And the total amount happens to be the 121 million dollars that's being allocated.
If I may, now, on IC-405, which is where we were just a minute ago. What 405 is showing you is that--and this top line starts off with the rate base and the allocation of the debt to capital which is 8614 which is debt and the cost of debt as being 8.287. And as you can see there, when a calculation is done, the debt is actually a hundred and six, 034.
Q. Just, for the record, I think that there may be an error in the statement of the rate base figure for that calculation.
A. It should be four, five zero, not four, three, zero.
Q. Thank you.
A. And if I may, the other thing that's wrong too

MR. ROBERTS:
is the reference is not JAB-1, page 1 of 94, that's what it was at the last hearing. It's actually RDG-1, page 1 of, I think, 107.
Q. That's the scheduled we looked to a moment ago -
A. Yes.
Q. - for Mr. Greneman's figures because this is Mr. Greneman's calculation, I take it?
A. This is the number of the interest that's shown and reflected in the cost of service.
Q. So the first two lines, that's Mr. Greneman's approach to get the figure that he got--he put in Schedule 1 of his -
A. Well -
Q. - cost of service.
A. That's the interest portion that shows within the cost of service, but it's also obtainable from one of the schedules that I actually have in my evidence when the calculation is done of the return on rate base, which is Schedule 4.
Q. Sorry, which schedule?
A. Schedule 4. Hydro's overall total rate base which has been calculated and shown on Schedule 3, and it comes to one billion, four

hundred eighty-five, four-fifty. So when you go back now to Schedule 4, within our rate base we have rural interconnective assets of approximately 213 million dollars, for which we only recover our cost of debt. On the other rate base assets, we recover our full weighted average cost of capital, which includes the cost of debt plus our margin. But at the end of the day, the full fourteen eighty-five, four fifty, from a debt perspective is what's included in the return on rate base. So this, back here on IC-405, the 1-4-8-5-4-5-0 that you see on Schedule 4 and what you'll see here on IC-405 is the same number.
Q. Yes.
A. And the 86.14 percent is just the debt to capital ratio and the 8.287, in this particular case, here is the cost of debt. So when you do that Math coming across, you end up with 106 million, 034. In addition to that, we also have work in progress and the Rate Stabilization Plan that are subject to being financed by both debt and equity. So based on the average balances of the work in

progress, which is as of 2003 and 2004, the average, and the same thing being done with the Rate Stabilization Plan and applying the same weighted average for debt, there's additional debt of 4.4 and 10.4 on those particular items. There are also assets that exceed the capital structure.
Q. I'm sorry, could I briefly interrupt you so I understand the source of those numbers. The CWIP, that's construction work in progress?
A. Yes.
Q. And the RSP is the Rate Stabilization Plan. The figures respectively of 62,351,000 and 146,220,000, did they come then from the balance sheet?
A. Yes, they would be balance sheet averages.
Q. They're the balance sheet averages from your Schedule 8 of your evidence?
A. Yes.
Q. Okay. Thank you. I interrupted you. You were about to go to--and these are additions to the -
A. These are -
Q. - interest costs.
A. - what's referred to as like a self-financing

asset. We incur the costs and set up the receivable for the Rate Stabilization Plan. We charge interest to that plan, so the interest is not an expenditure. We actually take it out of expenditure, put it on the balance sheet and we recover it from the customer over time.
Q. Okay. Thank you. I interrupted you a moment ago for that explanation. You were about to go to the next category.
A. The next one is a line that's referred to as excess of assets over capital structure, and if I may, if you were to add the rate base of there on line 13 of the 1.4 billion, plus the average of the construction work in progress and the Rate Stabilization Plan. The total of those three will come to what's there on line 18 of the one million six hundred and ninety-four thousand O twenty-one. However -
Q. So if the construction work in progress and RSP were reflected in rate base as assets, you'd get one million six hundred and--one billion six hundred and forty--ninety-four thousand--one billion six ninety four -
A. I'm saying rate base plus these two other

MR. SEVIOUR:
items are total assets that come to 1,000,694,021.
Q. Fine. I think I have your point.
A. So those three will add--this is our total assets. The RSP is an asset. So is construction work in progress and you'll find other assets within the rate base, besides the actual capital assets. However, if you look at our weighted average cost of capital, which is shown on Schedule 5 of my evidence, you will find here that the sum of total debt, plus the implied future benefits and retained earnings comes to 1,000,670,241. So we have a difference between the assets that are there versus what the capital structure is showing, and the impact of that when you're using the weighted average cost of debt here through the calculation is a reduction of 1,697,000. Therefore arriving at the net interest, the gross interest cost of 119 million 226. For financial statement purposes, we're recovering the interest costs--I should back up.
In the case of the Rate Stabilization Plan, it's financed with debt and equity. So

you will find, as we move down to Schedule--on IC-405, I should say, we are removing from interest, the impact of having these assets financed at the weighted average cost of capital. And the same thing is happening in the construction work in progress, is that these items are being capitalized into the project and will cease once an asset comes in service. So of our total interest bill of a hundred and nineteen, two twenty-six, we have it reduced by the amount of interest and financing charges that are associated with the work in progress that has been capitalized and added to fixed assets, and we have reduced it by the amount of the interest and financing charges that are associated with the Rate Stabilization Plan that's been added to the asset on the balance sheet and we'll recover from the customers over time.
In addition to that, you have a reduction for some interest earned on overdue accounts and the other one is just some timing differences as to when things are going through. So at the bottom, on line 28, what you're seeing here is this would be the

interest number that we would reflect within our financial statements, based on a total return on rate base as we have discussed earlier, of 121 million zero eighty-eight. This is the portion that we would be reflecting in our income statement and calling interest.
Q. And that's the figure that we find on Schedule 2?
A. That's the information that you would find on Schedule--my revenue requirement schedule, I think is 3 or Schedule 2.
Q. Schedule 2.
A. Schedule 2. So what you have is that if you added margin and interest together, that total equals what's done through on the calculations of the return on rate base. All this schedule is saying, here's how we would allocate those two numbers from a financial statement purposes between interest and margin.
Q. And is this, in fact, the calculation or approach that you used to get to the figure for Schedule 2?
A. This calculation that you see here, that's how we arrived at the 101 million that I have on

my revenue requirement. So the amount that I show for interest on Schedule 2, at line 34 and what you see here on IC-405 at line 28, that's how that's derived.
Q. Thank you. That is helpful, Mr. Roberts. I'm now going to ask you to turn up, with Mr. O'Reilly's assistance, NP-5, First Revision, which deals with the equity.
A. That does the reverse transaction of what we described for debt.
Q. And I think you probably need to take less time with that because of it, but I would like to go briefly through it, so that I can have this for our experts in some precision as to how this figure was achieved. The first lines 11 through 14, that's simply the same approach. This is Mr. Greneman's approach to achieve the -
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A. It's the same approach, except here what's being highlighted in this is that here you will find the split in the rate base. Whereas over on the other one, there is no split required because we recover the cost of debt on all assets. However, when it comes to

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margin, we don't earn a margin on rural assets. So consequently, from a margin perspective, we're not getting any margin here on the rural assets and that's why you'll find we've now shown here the actual split of the total rate base versus on the other one it wasn't required to show an allocation because you recover your full cost of debt on all assets. So on this one, in the line 11 to 14, you're seeing the assets for which a margin is earned and that's what gives you the 15,052 and that would be, as I mentioned earlier, that's also the same number now that refers back to RDG-1, I think it's page 1 of 7. So that's the starting point. Similar to what I had discussed of earlier in the review of IC-405 on the debt, the construction work in progress on the RSP are being financed at the weighted average cost of capital. That includes both debt and equity.
Q. And this is the equity portion you're showing here?
A. This is the portion that we're earning on those two particular assets. The financing on

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the overdue accounts and the excess assets also comes into play again here as well. So what ends up happening is that, on line 23, you end up with--this is a proof of the reconciliation of what will be reflected as a margin within the revenue requirement.
Q. In the part of the calculation involving excess of assets over capital structure, you use the debt percentage as opposed to the equity percentage. Perhaps you can explain that?
A. The rate that's being used there is the amount of excess assets for which there's debt assigned. There's no margin being earned on those particular assets. It's not traceable.
Q. So the issue of equity, an equity credit there does not enter into the calculation?
A. That's correct.
Q. And the final adjustment that's made here is the issue of differences due to timing of cash flows?
A. Yes.
Q. What's that all about?
A. I think what I'm trying to explain is, for instance, what you're looking at is really the

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reference into the way that we're using thirteenth-month lags and we're using Lead Lag study, but we're actually doing interest on a month-by-month calculation basis. So by using averages versus actually a month-by-month calculation, you get some timing differences as to how things arrive.
Q. Mr. Roberts, I'm glad we're doing this early in the day.
A. So am I.
Q. I have one final piece of the puzzle which still remains somewhat of a puzzle to me, but hopefully will not to my experts. But, the final IC I wanted to refer to in this area is IC-406, and in the two previous ICs that we looked at and these calculations that you've taken us, you know, so comprehensively through, you've referred to the excess of assets over capital structure and this IC, No. 406, is directed specifically to that concept and that calculation, and I did have a few questions, before we left this area, about this, both at a conceptual and at a calculation level. Maybe we'll start with conceptual. First of all, can you explain,

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for the benefit of ourselves and the Board, what is the concept of excess assets over capital structure? How do you get such an excess?
A. Maybe I can, just by using what's here, try to explain by using--I'll just start initially with the fuels and supplies. For the purposes of rate base, the accepted methodology of calculating a rate base is that in the case of inventories, you normally at a thirteenth-month average and that will be different than if you happen to pick two specific points in time, which is what your financial statements are based on. So for rate base purposes, it's normally used and generally accepted in the calculation of rate base that you would use a thirteenth-month average, and I, for the minute, can't recall the full logic behind it, but if you would remember to ask Ms. McShane who provided the assistance and advice to us in developing the methodology that we should be using for rate base, I'm sure she'd be able to tell you the true logic behind thirteen months versus using simple averages of just the two years. So as you can see there, if

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you had just used the balance sheet comparisons, the average was 33,719,000. By using a rate base, which assumes a thirteenth-month average, and I think the intent was to eliminate a high and a low period in using the thirteen months, rate base actually has 34,294,000 for a difference.

It's also quite common in calculation of rate base is to make an allowance for working capital. You do have ongoing financing involved from the time that you bill customers, by the time you pay, time lags in when you pay your suppliers versus other aspects that are happening, and it's very normal, in doing a rate base calculation to have a provision in there to allow for this cash working capital. And historically, these are done on what's referred to as a Lead Lag Study where you will actually look at your revenue and say "well, I bill here. How long does it take and it's in the system and before I actually get paid?" and look at your expenditures on the same line, "when do I incur the costs and when do I pay it?" and

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then based on that, arrive at a percentage that will be applied to your cost and determine a working capital number that will be included in rate base for which you would be able to earn a return on.

The five items that you see listed here accounts receivables, prepaids, accounts payable and accrued interest, are what you're trying to cover off by having a cash working capital allowance allowed into rate base, because, you know, every month, things will change and what they're trying to do is to provide funds through the organization to do this financing while you're waiting for receipt. If you were to look at what actually happened, if you were to look at the projection of specific balance sheets at three and again at four, you find a completely different result. There you'll find a negative of 20 million dollars versus the rate base as being in there as 3-0-5-7 (phonetic). So you really have a net swing there of 23 million 205 when combined with the fuel and supplies. That's the 23,780,000 and that's what's contributing to this difference when we

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refer to it as the excess of assets over your capital structure. Because when you add up the rate base, which would include allowance for these fuels and supplies and net working capital, and you add your work in progress and you add your RSP, in reality, you have the asset side of your balance sheet. But when you look at your weighted average cost of capital calculation, which is the other side of the balance sheet, your liabilities and your equity, you have this difference, and the difference arises because of using different methodologies to be included, and then the example there is you're using inventory at thirteenth-month averages rather than simple averages of two years, and in the cash working capital, you're not using specific balances as of three and four. You're actually doing a separate Lead Lag Study where you're looking at each component to arrive at what should be a reasonable level of cash working capital to allow into rate base for which you would be entitled to a return on. So I don't know if that -

Q. That's somewhat helpful. I just want to take

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it a couple more steps. In the figures that we have on IC-406, the three first columns of figures for 2003/2004 on average, they're balance sheet columns?

A. These are straight balance sheets and they should flow through from -

Q. Yes. They correspond, I think, to your schedule.

A. - schedule, I think it's Schedule 8 again.

Q. Yes. And then we have the rate base figures in column four. Column five, as I understand it, is intended to be the rate base minus the balance sheet figures?

A. Yes.

Q. Reflecting ultimately that there's $575 excess on account of fuel and supplies.

A. That's 575,000.

Q. 575,000, I'm sorry, of course. And then 23,205,000 -

A. Yes.

Q. - on account of the four other categories?

A. Yes, for the cash working capital allowance.

Q. And the figure that we come to, $23,780,000, that I take it is to represent the amount of excess over the capital?

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MR. ROBERTS:
A. That's the excess of assets over what our capital structure is by making those comparisons.
Q. Okay.
A. And then when you apply the cost of debt to that, that's where we end up with that credit of 1-6-9-7 that was reflected earlier on IC-405.
Q. And if I take you back to IC-405 for just one brief moment, if we move down the screen to the excess of assets over capital structure, the difference there, the 1.694 billion minus 1.670 billion, if you do the math on that figure, I think you come out to the $23,780,000 which is -
A. Yes, that's the 23,780,000 that we just talked about in IC-406.
Q. Okay. Just a couple of final points on this schedule. On the balance sheet item, the fifth line, the accrued interest figure, can you help us on what that represents? We're back on IC--I'm sorry, IC-406, Mr. O'Reilly.
A. Okay. Just bear with me for one second, if I may. Mr. O'Reilly, can I ask you to go back

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to IC-238, page 3 of 3? To provide you with some information as to what the accrued interest is, if you looked at our long-term debt issues that we have here, interest is payable semi-annually. So what you will find is that if the interest, and I'll just pick one and use it as an illustration only. For instance, if you picked the last one that's there, the 6.65 percent, the maturity date is 27th day of August, 2031. The interest would have been paid semi-annually on that particular bond issue. So we would have accrued, in either 2003 or 4, depending, the interest that would have been applicable from the last payment to the end of the year. So that would be done for all of these particular bond issues. So we would still have a full twelve months accrual of interest within the particular year. That's what the accrued interest would represent.
Q. Prior to dispersing it in payments?
A. Yes. We would make the accrual on a month-by-month basis until such time as when it was paid and then the payment would just offset the liability that we have already required.

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Q. And is this the issue that Mr. Drazen addressed in the 2001 GRA?
A. Mr. Drazen's issue that he was raising was assuming that we were having the use of all this interest for a period of time, which in fact is not correct because of the fact that our interest calculation and the interest run we do is an iterative process. So what it does do on a month-by-month basis, it literally factors in the impact of receiving these funds and receiving the interest on a month-by-month basis. So that was taken into account in doing the calculation of the interest run.
(10:00 a.m.)
Q. And just to, finally on this IC-406, and that's a helpful explanation, Mr. Roberts, the final line of the exhibit refers to net cash working capital and I take that to correspond to the figure of $23,205,000?
A. That's the average of the 2003/2004 for those categories beginning with accounts receivable and ending in accrued interest, less or plus or minus the adjustment relative to rate base to see what the difference is.

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Q. I was interested in your description of that figure, the net cash working capital. Are we to take it that this represents an additional source of working capital which is not reflected on the rate base?
A. Yes, because of the fact that the rate base, the amount that's included in rate base is based on a Lead Lag Study.
Q. Yes.
A. What you're seeing here is an actual comparison at a point in time, which are two different methodologies, giving you two different results. But what that would imply, if that was the case then, is that we have availability of funds to be used for other purposes.
Q. Thank you, sir.
A. But it's only of a short-term nature.
Q. I want to talk to you--take you briefly to Exhibit JCR-1, Mr. Roberts, somewhat related question, and this is entitled Cash Working Capital Allowance, Analysis of Semi-Annual Long-term Bond Interest Payments, and this is your document, I take it, is it, Mr. Roberts?
A. Yes, it is.

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MR. SEVIOUR:
Q. And does this address the issue that you just covered off in returning to IC-238?
A. Yes.
Q. Okay.
A. This is illustrating the impact of the approach that was being referred to by Mr. Drazen and illustrating the way that through Hydro's iterative interest model what the actual impact happens to be.
Q. Yes, and as I understand your conclusion, and I think I have your point that notwithstanding that Hydro does receive payments on account of ultimate long-term debt payments in advance, through its rates, and it does receive earnings on those advance payments, that Hydro adjusts for this in its reported cost of debt?
A. Yes, this is reflected back through in the calculation of the interest run.
Q. And the weighted average cost of capital -
A. Yes.
Q. - which feeds into the cost of service?
A. That's correct.
Q. So that there is an adjustment?
A. So it is taken care of when you go back

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through the detailed interest run. It does reflect it.
Q. One question I had and it's a fairly simple one, if we turn to Table 3 at page seven of your report. This details the identification of the timing differences that you adverted to a moment ago, I think. Is that fair to say?
A. Yes.
Q. We're looking at, particularly in the third column, investment account earnings which I take it to reflect the investment accruing to the earlier than required payments on account of the long-term debt?
A. Yes, this is reflecting the payments on a month-by-month basis and the imputed amount of interest that would be reflected through the interest run.
Q. And in the example, which I think is all just illustrative, we show that in a year by reason of these month-by-month payments, there is an accrued balance of $5,326 standing in the investment account?
A. Yes, and that's -
Q. In your hypothetical?
A. Yes, and that's what's used then to help

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retire the debt service.
Q. And that's my question. What, in fact, becomes of those funds? How are they applied?
A. Well, what you're calculating is the interest that you would have from doing this and it's just reducing the interest costs that will be determined by having the availability of these funds. So it reduces the short-term debt requirement for which interest will be added to or subtracted from.
Q. Okay. I think I understand your point. I just have a couple of final points to conclude, Mr. Roberts. You recall yesterday we looked at a number of quarterly reports that included forecast income statements. I don't plan to take you to them, frankly, sir. If you'd like to turn them up, I'd be happy to do that with you. It's WW-1 and WW-2, I think. And these reports reflected, as I understood it, in the income statements reviewed with Mr. Kelly, they reflected moving forecasts as against actuals year to date for each quarter?
A. Yes, with the caveat, as I had mentioned, that in normal circumstance is that we would have

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done a forecast in the April period which would have been reflected in the June results. Any forecast that would have been done in the first quarter ending March 31st, 2003 would be negligible at that point. As I mentioned, we have a mandatory review period for a complete review of all costs and that's done in April, in consultation of the normal time that you would be doing your budget, and also again, in late September/early October as you're trying to finalize your next year's budget and your most recent forecast for the current year. In light of the way that 2003 was elevated for purposes of filing this application, we actually did a final review of the 2003 results in December of 2002 and then another final look in February of 2003 because it takes six to eight weeks to take these numbers and churn them through rates and do iterations and come back and recognize that you're still doing evidence, but you don't have final numbers until all this iteration and rate design is done. So your cut-off point for 2003 was basically in around about February of 2003. And consequently, in light of that, a

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MR. ROBERTS:
decision was made that we wouldn't be doing an update in April because the update relative to 2003 would be done in the fall for this hearing. So the decision was made to wait and do it at that time, rather than to try and accomplish one and then have to go back and revisit everything again. We decided that we would only do one.
Q. When we went through this in the exercise of your discussions with Mr. Kelly on these reports, it occurred to me that it would have been helpful if the reports reflected the budget for the year in question, in addition to the information that's currently reflected in them, and I just wanted to get your reaction to that.
A. I guess if the Board so desires to have the annual budget reflected on the reports, we can quite easily accommodate that request. What's being presented now has been, I guess, through agreement and discussion with the Board as to what they would like to see, but if they were interested in seeing what the annual budget was and how the annual forecast is moving in

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relation to that, I don't think it's a major job to add another column to it and put it down. The budget amounts stay as the budget for the whole year, so if it's of value to the Board, I'm sure that we could accommodate that. (Undertaking)
Q. Thank you. I wanted to conclude by discussing the return on equity that's being sought on this application by Hydro, and that's a return on equity of 9.75 percent, which represents an increase from 3 percent from the last general rate application. Is that correct?
A. Yes, it is.
Q. If we look at your Schedule 2 for a moment, the return on equity that is sought is shown in line 35 at a total amount of 19,384,000, is that correct?
A. No, I'm going to take you back to our discussion this morning.
Q. Sure.
A. This is the allocation of the return on rate base into the components that we require for an income statement. As you'll recall from our discussion this morning, what rates are being based on is the amount that's in Mr.

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Greneman's cost of service, and I think the number is 15 million dollars.
Q. 15 million.
A. Okay, this is just an allocation of--what you're seeing in my revenue requirement is an allocation of that total rate base between interest and margin, but what's actually used for rates is what's included in Mr. Greneman's evidence, which is there on the screen, which is the 15,052.
Q. And do you know or can you tell us, and perhaps--no, I'll leave that question for another witness, Mr. Roberts. Thank you, Mr. Roberts. Those are my questions.

CHAIRMAN:
Q. Thank you, Mr. Seviour. Thank you, Mr. Roberts. Good morning, Mr. Kennedy.

MR. KENNEDY:
Q. Thank you, Chair.

CHAIRMAN:
Q. Do you have any idea if you'll be approximately how long?

MR. KENNEDY:
Q. I wouldn't suspect it'll be more than an hour.

CHAIRMAN:

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Q. An hour or so.

MR. KENNEDY:
Q. Certainly, I'll bring us to the break at 11, if that's appropriate.

CHAIRMAN:
Q. I was thinking it would appear we might finish early today, so I'd like to take the break at quarter to, if that's okay with you.

MR. KENNEDY:
Q. That's fine.

CHAIRMAN:
Q. If you could zero in on that.

MR. KENNEDY:
Q. Sure.

CHAIRMAN:
Q. I'd appreciate it. Given the nature and content of the discussion this morning, we might all appreciate 15 minutes early.

MR. SEVIOUR:
Q. For that, I take some responsibility and apologize, Mr. Chairman.

MR. KENNEDY:
Q. Well, I canvassed all the funny stuff in the application last night. Mr. Roberts, when you testified on October the 14th--I wonder if,

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MR. KENNEDY:
Mr. O'Reilly, you could just pull up that transcript, on page 13, and interesting enough, similar to my review of transcripts with Mr. Wells, this happens to be a passage where you're getting some well-phrased questions from your counsel, and they're equally well-phrased replies. And in particular, at line 11, your counsel referred to the report of Grant Thornton and how Grant Thornton made certain observations with respect to Hydro's history of spending on its capital budget. And "will Hydro be factoring any allowance in the calculation of its rate base to provide for potential under spending of the capital budget in the test year?" and we know generally what that issue involves, as a result of the exploration of the issue in the 2001 hearing. And your reply was that "Hydro has steadily improved its record with respect to meeting its capital budget and has reduced the percentage of under spending by 50 percent from 1998 to 2002." And you say "in 2002, even given the late approval of the capital budget, Hydro's total under spending

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was less than 10 percent."
(10:15 a.m.)
So I guess to the person just reading that, on its face value, it could imply that Hydro is motivated to spend all the capital budget that's approved, just so that there won't be a discrepancy between the approval and then the actual expenditure for the purposes of what goes into the rate base for the test year, and I don't imagine that's what you meant. So I wonder if you could just elaborate on this point for us. How is it that Hydro's achieving this reduction in percentage of under spending? Is it in the application process itself, or is it in the -
A. We're getting better in completing the projects on time and within the year in which they were budgeted to be completed.
Q. And on previous occasions then it was the case of Hydro's, some of Hydro's spending on its capital budgets would be carried over into the next year?
A. Yes, that's, in fact, correct. And in the case of some of the projects such as a multi-year project, it could be just a function of

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cash flow as to when the costs were actually incurred versus the work. But in total the project would still be completed within budget.
Q. The other question I wanted to ask in relation to this was just some general questions about Hydro's policy regarding the booking of expenses, vis-a-vis whether they're operating or capital. And if we could turn to Grant Thornton's report of 2003? Page--we'll start at the bottom of page 41, Mr. O'Reilly, just so we can get the heading so the witness can see where we are. Mr. Roberts, page 41, yeah, there we go, at the bottom there this is a section on a discussion that Grant Thornton did on the system equipment maintenance budget category. And then if we go to the next page, Mr. O'Reilly? Here we go. And there's a breakdown there of the figures per transmission and rural operations, production and so on. The next paragraph at line 2, "In 2002 there was a significant increase in the TRO division which was primarily due to certain non-recurring extra maintenance cost in the central and northern regions. The

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extra maintenance requirements in these areas included inspections and replacement of wood poles, reconditioning transformer oil at the Bay d'Espoir site, repairs to air blast circuits at Sunnydale (sic.), repairs to diesel units due to a leak in the exhaust manifold, radiator and generator failure and an overhaul on diesel unit." Am I gathering correctly that Grant Thornton's referencing these items that they are, in fact, or have been booked by Hydro as operating expense items?
A. Yes.
Q. And if that's the case, could you explain why, for instance, the replacement of a wood pole would not be considered to be a capital item?
A. There's a question of materiality that would come into play onto what would be capitalized relative to wood poles. For instance, we look at a line in total. If we replace a major portion of the line, then we would capitalize it. But if you're replacing a pole here and a pole there, we would not. So the line itself is the total unit of property in the asset. So if the line happens to have 500 poles and

MR. ROBERTS:
there's three or four broken off, we would not capitalize them, we would not try to write out the old and find a way to capitalize that.
Q. So the treatment of whether it's capital or operating is based in part on the nature of the -
A. There's an element of judgment that's exercised in the work that's done as to whether or not it would represent a significant portion of the line.
Q. Okay. So in the case of poles, only if it's a substantial improvement of the line -
A. A substantial improvement that's going to impact on the line. The replacement of a broken pole within a complete line structure would not be capitalized.
Q. Okay. A little later down on the same page, the second-last paragraph, yeah, there's reference there to production department and maintenance costs have been forecast to increase. There's an explanation then that goes on concerning Holyrood. And then these projects include heat tracing refurbishment. You see where I am?

A. Yes.
Q. And one of them is roof replacement, $215,000?
A. Yes.
Q. So again, am I gathering correctly by Grant Thornton's discussion that expenditure for roof replacement was booked as an operating expense?
A. Yes, it was.
Q. And could you tell me why that would have been booked as an operating expense instead of a capital expenditure?
A. I think you'll find that the roof replacement was only a partial replacement and we would be looking at the total building as a whole. Like, the replacement of a partial roof is not going to change the--is not going to extend the life of the building as a unit.
Q. Okay. So -
A. So it would be like replacing the shingles on your roof, you know, your house is still good for 40 or 50 years and you anticipate over that period of time that you may have to replace your shingles two or three times. In this particular case there was a partial replacement on the roof.

Q. Okay. So that's the key is, it was a partial replacement?
A. Yes. And most of these it's a function of looking at what the work was done in relationship to the asset that's there and then that will help dictate as to whether or not it should be capital or operating.
Q. So if it was a complete replacement that extended the life or was expected to extend the life of the building, then it would be booked as capital?
A. Yes. If it impacts on the remaining life.
Q. And that's a judgment made by you on advice received from engineers?
A. That would be through the staff that do work for me based on the information that would be provided from the individuals that are raising the capital budget proposals and subsequently a capital job cost to complete the work.
Q. Okay. The other curiosity was at page 45. And this was under the professional services section of Grant Thornton's discussions. And it's the second-last paragraph on that page, the forecast fees for software acquisitions.
A. Yes.

Q. In 2003 and 2004 are above 2002 levels. There is an increase of 65,000 in 2003 and another 73,000 in 2003. "Hydro advises that this is due to the escalating prices for the cost of software."
A. Yes.
Q. Could you just tell us what your policy is regarding the booking of software expenses as operating versus capital?
A. Our point in which we would capitalize new software is $25,000. So anything less than $25,000 we do not capitalize. And in the case of licences, they are expensed, we do not capitalize them.
Q. And so are there other items that--or categories of expenditures that are determined to be operating versus capital based on the amount of money that's being spent other than the one you just told us, software?
A. I think there are materiality limits that we would look at in various areas of expenditures. Just trying to go from memory now.
Q. Is the materiality trigger a proxy for when the asset that's being purchased would be

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MR. KENNEDY:
considered to be -
A. Whether or not it's a substantial benefit or improvement to a particular facility and whether or not it's just a component of a unit.
Q. Because certainly Hydro does apply for approval as part of its Capital Budget Applications process for the acquisition of software, so there are instances where it is treated as a capital item?
A. Yes. But they would have to be in excess of $25,000.
Q. Okay. So now the increases here are above 25,000, 65,000 in 2003 and 73,000 in 2004, but that -
A. I can only assume that -
Q. - must be busted up, up among a whole bunch of different items?
A. - that will be a combination of several items that would accumulate to the 65 and the 73.
Q. Okay. Is that similar then to if we go over to page 47, and this is in the other cost category and it's the second-last paragraph on that page. Begins with "The increase in

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equipment rentals". Do you see where I am?
A. Increase, yes.
Q. Okay. It says, "The increase in equipment rentals is attributed to the increase in cost of leasing communication circuits, interconnection costs and some licensing costs." And then it goes more specifically, "There is an increase of computer costs of 109,000 from 2002 to 2004. This is due to the increase in computer costs mainly related to the extra disc space required for the disaster recovery plan." So again, was that an operating expense as opposed to a capital, and if so, why would that have been the case?
A. We have actually leased extra disc space to the disaster recovery at an off site location and that's why there's an increase in the cost of storing that information on somebody else's site. We don't actually own the disc space, we're actually renting the disc space to store our information as part of disaster recovery.
Q. Okay. And that's not treated as the capital lease?
A. No.
Q. Okay. I wonder if I could just turn to just a

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more general discussion about the rate base itself? And if we could pull up P.U.B. 110, please? I just wanted to make sure we have this up first, Mr. Roberts, so we could provide the segue, if you will, for the discussion. And this was the question that was put to Hydro about its intention to conduct a valuation of its rate base?
A. Yes.
Q. Okay. And so that it could be fixed and determined in accordance with Section 64 and 68 of the Public Utilities Act. And then there's a reply, if we could just scroll down, it reference the Hydro Corporation Act 17(2). And then if we could just scroll, I think that's the last of the answer, but it says, the last sentence, "The legislative direction found in subsection 17(2) the Hydro Corporation Act precludes and obviates a valuation of Hydro's rate base under Section 64 and 68." So that's the Company's position regarding the fixing and determining its rate base, correct?
A. Yes.
Q. Okay. And we'll leave the legal

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interpretation to the lawyers. But I wanted to ask you then some general questions about your rate base itself in light of this position. The first thing, though, one of the things that caught my eye in the Grant Thornton report, the same one we were looking at, the 2003 GRA Report was at page 18. And it's in the bullets, it's that last bullet there, it says, "2002 retirements were adjusted for 1.1 million associated with the fire loss at Rencontre as well as 4.2 million related to the write off of assets at their Holyrood plant as a result of a physical verification of assets." Now, were they--they were capital assets?
A. Yes, they were.
Q. Okay. And could you just give us a little bit of background on what took place there?
A. The numbers that you're seeing here is the original capital cost. So the $1.1 million is the original capital cost of the assets that were destroyed at the fire at Rencontre East. And -
Q. Yeah. Actually, I probably should have made it clear. I wasn't concerned with Rencontre

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MR. KENNEDY:
East, I was more -
A. You were concerned about Holyrood?
Q. Yeah.
A. Well -
Q. Wondering how is it--what was the process that Hydro employed to get to that?
(10:30 a.m.)
A. Yes. I'll just come to that. And the same answer is there, that the $4.2 million worth of assets at Holyrood is the original capital cost. The actual net book value of the assets that were written off is $800,000. And that arose as outlined by Grant Thornton in their report. One of our process reviews that we are in the process of undertaking is matching all of our physical plant records to every single piece of equipment that exists out into the field, and we're doing it location by location. When the verification of Holyrood was done in 2002. It was discovered on the physical count that we had certain records recorded within our capital assets for which they had been disposed and as a result the adjustment of $800,000 had to be made in 2002.

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Q. So the 4.2 million original cost assets that were written off, would that have been a combination of items that were obsolete and items that just weren't there?
A. From going from memory it was a difference of--we did an actual physical count of the assets, we matched them to our fixed asset records and what we discovered is that when we received the disposal form from the area saying they disposed of an asset, of course, you got different terminology that's being used. And we wrote out what we thought was exactly what they did, but the physical verification says no, there were some other records that we had called something different than what the field was, but was exactly that same particular asset and should have been written off.
Q. Okay.
A. So, like, for instance, in this particular case the impact on rate base is not $4.2 million, the impact on rate base would have been whatever that net book value is that -
Q. The 800,000?
A. Yes. Or -

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Q. Yes, yes. This process that you described of matching all your physical plants to the actual field conditions, your physical plant records to the actual field conditions, when did Hydro embark on that process?
A. It really commenced in late 2002 with Holyrood being the closest place to tackle first and to extracting information from our financial records and then by utilizing finance resources and resources from Holyrood, start matching what was in their equipment records at the plant versus our financial records and try to do the match one to one or one to many, whatever the ratio happened to be. And once that was accomplished, then to investigate what was left over on both sides to see if something can be found as to whether or not there was something that should have been recorded or if there was, in this particular case, some assets that should have been written off at an earlier date.
Q. How long will it take Hydro to complete this process that it started in late 2002?
A. It's going to be out in early 2004 before we finish the process. Just to give -

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Q. Early next year?
A. It'll be out into early next year. And the reason why I say that is that I know from a financial perspective recorded in our financial records we have 35,000 records. When you go to the various areas, of course, that multiplies significantly because I may have a generator at Holyrood or a generator at Bay d'Espoir as one unit, whereas within their equipment records that may be multiple pieces of equipment. So you're trying to do that match and tie up what a fixed asset record is and what's the other side of the equipment record so that process is ongoing, as well as to identify any additional items that should be either added or deleted from the fixed asset records.
Q. Does this review that's being conducted as you describe it include any elements of a determination of the--whether the asset on an asset-by-asset basis is still used or useful?
A. Yes, it will, because we're dealing with the plant who know these records and if they're not being used, then they would provide that information to us.

MR. KENNEDY:
Q. Is that implicit in the process?
A. That's implicit in the process.
Q. So it's an--and so the reverse of that, it's not--is it fair to say it's not an expressed initiative by Hydro to conduct a review of its assets to determine whether each and every one of them that's in the rate base is used and useful?
A. No, that's not the idea. The objective is to match financial records with equipment records and to identify any differences and make the appropriate adjustments if deemed necessary.
Q. Now, in your Exhibit JCR-2, page 1, this is your report on the non-regulated operations, Mr. Roberts?
A. Just give me one second.
Q. Okay.
A. So many binders it's -
Q. Yeah. You need a computer. Right in that first paragraph you indicate in this exhibit that "All costs associated with any asset which is not used and useful in the generation transmission and distribution of electrical power and energy by Newfoundland and Labrador

Hydro within the Province of Newfoundland and Labrador activities exempted by specific legislation and costs specifically identified by the Public Utilities Board as being non-recoverable from ratepayers." So that's your definition of non-regulated operations, correct?
A. Yes.
Q. All right. So you recognize that in this jurisdiction for something to be approved from a regulatory perspective to be in your rate base it must be used and useful in, in your case, the generation, transmission and distribution of electrical power and energy?
A. Yeah, it has to be used and useful in those areas of our activities.
Q. Okay. I wonder if we could go to NP-91, please, Mr. O'Reilly? And you just--I think it's two pages over, so page 3 of 4. This was the question asking you to provide some details concerning the calculation of plant investment and rate base?
A. Yes.
Q. And there was some questions I had just in relation to this. One is you have a line item

there, No. 19, non-depreciable land plant. Could you just explain what that is?
A. It should represent the value of land which is not subject to depreciation, but yet, within our category of plant it's there as a separate item.
Q. So would that be vacant land, then?
A. No. That would be all land, the land at Holyrood, if we happened to own it, and land is not a depreciable asset.
Q. So in the case of general properties, that's just the building infrastructure, correct?
A. It's general properties. You know, your buildings, things that are subject to depreciation. But land is an un-depreciable asset.
Q. Okay. Could we just scroll one more page? This is a continuation of the same -
A. Yes, I'm familiar with it.
Q. - charts just brought forward. So we start off with the plant investment less your work in progress?
A. Yes.
Q. Right. And then you deduct certain amounts here. And you've got line item 32, "Add,

deduct other items."?
A. Yes.
Q. Could you just tell us what that is?
A. That item in particular here that you're seeing here is some assets that are related to Muskrat Falls in Labrador.
Q. Okay. Mr. O'Reilly, you can keep that handy because we're going to come back to it. If we could just go to Schedule 3 of Mr. Roberts' testimony? So, Mr. Roberts, this is again, I guess, sort of just a restatement of some of the same information to get your rate base figure. And you can see we've got the total capital assets and then less the contributions and aid cumulated depreciation. Then you have Muskrat falls and then assets not in service. So that's what you were indicating previously?
A. Yes. So your twenty, eight-four that was back here in NP-91 is the twenty, ten, plus the seventy-four.
Q. Right. And I understand Muskrat Falls a non-regulated activity -
A. That's correct.
Q. - and so it gets excluded from your rate base. What are assets not in service?

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MR. ROBERTS:
A. All I can tell you is that somebody has done a review of the plant balances and these records are not in service and had been removed from the cost of service. As to what makes up a 74,000, I honestly couldn't tell you at this point.
Q. So would that in any way relate to a use or useful or is this just sort of a plug to -
A. No, this is not a plug. This would be based on identification of specific assets that are not in service and not being used.
Q. And so is there a person in Hydro responsible for doing that, for -
A. This is one of the exercises that we would form part of completion of the cost of service. The staff members that are preparing the cost of service go through the detailed listing of the fixed asset records and within our system. For instance, as we take a vehicle and we take it out of service and we park it in the yard and wait for a disposal, within our financial records in fixed assets we would change the category number on that particular asset, say, from a one representing

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an operating asset in Holyrood to a Code 7 which is an asset held for disposal. So, when the staff preparing the cost of service go through fixed assets, they look at the categories of the assets, and what the assets not in service should represent are assets that we have on hand at net book value at this particular point in time that are held for disposal or for sale or not related to being used and useful in the operation.
Q. So now the--so a couple of questions. One is, so in relation to Hydro's proposal on rate base that you have an average rate base of one billion, 485,450 for your test year?
A. Yes.
Q. All right. And that--and am I gathering correctly then that the only line item that is provided in any of your filings from what I could see regarding assets not in service to quantify them for which you do not get a rate of return on that it's this, in the case of 2004, this 74,000?
A. Well, it would be the 74 plus the twenty, ten for Muskrat Falls.
Q. Yes. And Muskrat Falls, it clearly, it's an

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asset though that's quite used and useful, but it's non-regulated?
A. Yes, but it's still in our plant records, so we still removed it so that it's not being figured in with the rate base.
Q. Now, you, I believe--and we don't have to go to it, but just for the Panel members, NP-101, you make an adjustment in your interest rate calculation to take out the interest on assets not in service, correct?
A. Yes, there has been an adjustment made.
Q. Okay. Now, the next item I just wanted a quick question on was your cash working capital allowance. You've got booked at 3,057,000 for your 2004 test year, correct?
A. Yes.
Q. And that cash working capital allowance is based on a formula, it's a percentage of various other figures, correct?
A. Yes. It's, I believe it's -
Q. It's in your--it's in one of your schedules, actually.
A. It's a percentage, I think it's 5.23 percent or something like that -
Q. Yeah, I think it's for three percent and two

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and a half percent, depending on what asset class you're obtaining your working cash allowance for, correct?
A. It's based on the analysis of the Lead Lag Study associated with the revenue and the same principal being applied to cost as to the lag that's required there and then factoring in the impact of what HST does to the availability of funds as well because you do have some utilization of funds on the timing of when that's paid, as well.
(10:45 a.m.)
Q. IC-406, if we could, Mr. O'Reilly. And this was a response that--well, it's a question directed to yourself concerning the excess of assets over capital structure and then sort of a reconciliation of some of the figures. And as was explained in your answer, your balance sheet figures may not necessarily jive with your regulatory filing?
A. That's correct. There can be a difference because here you're looking at an absolute point in time versus different methodology to calculate an amount for rate base.
Q. Sure. And in your case of your balance sheet

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MR. KENNEDY:
there's a net cash working capital line you have there?
A. Yes.
Q. For 2004 of 15 million, 246?
A. That's the sum of the balances as of 2004.
Q. So am I gathering correctly that for the purposes of--and you see then you've got an average of 20 million, 148 as between 2003 and 2004, correct?
A. That's correct.
Q. Okay. And then we see this 3,057,000 figure which is your actual rate base provided working cash allowance?
A. Yes. That's the results of what happens when you go through and do the Lead Lag Study.
Q. And then the difference is 23 million, 205, that's -
A. Because one is negative and one is positive, yes.
Q. That's the swing?
A. Yes.
Q. Am I gathering correctly then that conceptually, according to your balance sheet, Hydro has adequate provision for its working

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capital in that according to your balance sheet you had an average of 20 million, 148 in working capital available to you?
A. What I've shown you is that by picking the actual balances as of three and four, this is what the results will be. But what has been done is the Lead Lag Study, which is common in the preparation of a rate base, and that's looking at the individual components of the revenue and the cost to try to determine what it should be. So it's trying to show that two methodologies here have different results. The same thing would apply to inventory, if you're just looking at simple year end balances on an average versus the norm of using 13 months, that gives you a different results. Of course, that also impacts on when you're trying to do your reconciliation of your total return on rate base in relationship to how you would allocate between interest and margin.
Q. That's a good place to pause, Chair.
CHAIRMAN:
Q. Thank you, Mr. Kennedy. Thank you, Mr. Roberts. We'll reconvene at quarter after.

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(BREAK - 10:48 a.m.)
(RESUMED - 11:20 a.m.)
CHAIRMAN:
Q. When you're ready, Mr. Kennedy.
MR. KENNEDY:
Q. Thank you, Mr. Chair. Mr. Roberts, I just have a couple of more questions concerning the Rate Base issue, just before we move on from that. And it's indicated in IC-10, and if we could just go--and before we do that actually, this was again a question directed to Hydro by the Industrial Customers asking for actual costs of the Island Interconnected system.
A. Yes.
Q. Okay. I wonder if we could just go the next page, there we go. And I'm interested in line 34, Mr. O'Reilly, so you can--there we go. And these, again, are details concerning the revenue requirements of Hydro for just the Island Interconnected portion of your cost of service, as I understand it. And the line, item, 34 there, write down of capital assets. And am I gathering correctly that if we go through from 1997 through to 2004, although there's years missing in between, that it

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would appear that there's been no write down of capital assets by Hydro throughout that entire period?
A. That's correct. Line 24, write down of capital assets, if memory serves me correctly, was related because this is just a template that's used. What that line referred to, going back in time, I think was the write off of the Roddickton Woodchip Plant.
Q. Okay.
A. And it was shown as a separate item, rather than being up as part of line 26 where we say loss/gain on disposal of capital assets. Line 34, back in history, in the year in which it was done, the write down and write off of the Roddickton Woodchip Plant was shown as a separate line item.
Q. So, that's just a hold over from -
A. That's just a template that was used and the lines were there and unfortunately, it should have been probably removed.
Q. Now, am I gathering correctly from a review of CA-59, and just for your reference page 40 of 223, these are the annual reports of Newfoundland and Labrador Hydro. And there

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MR. KENNEDY:
was no line items--I'll just find the reference there. Can you just scroll down? Scroll down some more, please? That's the problem without line items, then you can't find--the question I had, I just wanted to confirm that there was no provision in Hydro's Rate Base for decommissioning and site restoration and is that a policy that the company has?
A. The policy does exist and it will be dealt with on assets as new assets are being built, if it's deemed appropriate.
Q. So, in the case of, for instance, Harbour Deep, as I understand it, Hydro, when it decommissioned the plant in Harbour Deep, it actually was still able to use the diesel generators that were at Harbour Deep and other locations in the Province, is that correct?
A. To the best of my knowledge, they were removed and will be used elsewhere.
Q. Was there decommissioning costs and site restoration costs associated with the closing of the Harbour Deep facility?
A. Yes, there was.

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Q. And then that would be an additional capital expenditure that you would seek specific approval for by the Board?
A. The criteria under the decommissioning costs was as set out in the depreciation study and there it was based on a dollar value. And if memory serves me correctly, if it was less than a predetermined dollar value, then it would be expensed in the year in which it was done, rather than to be capitalized.
Q. But in the case of, for instance, Newfoundland Power had a steam generating plant in St. John's here, are you familiar with that?
A. I know they had a steam generating on the South Side, yes.
Q. Used to have a steam generating plant on the South Side. In the case, as I understand it anyways, in that case as I also understand it, there was, as part of the depreciation of that plant, after it zeroed out, after the plant was fully depreciated, there was, in actual fact, a continuing depreciation on the plant to provide provision for the decommissioning and site restoration work that was expected on the plant, but Hydro doesn't do the same thing

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in it's budgeting?
A. No, it does not.
Q. Okay. Mr. Roberts, is the last depreciation study that Hydro has obtained is the KPMG study of 1998?
A. Yes, it is.
Q. And could you tell us when that will be updated?
A. By order of the Board it's either 2004/2005, whatever is in P.U.7. I'm not sure right now if it's four or five, but there is another one that is scheduled to be completed.
Q. I just want to turn to, now, your return as applied for. And Hydro is seeking a Rate of Return on Rate Base of 8.15 percent in the revised filing, correct?
A. Yes.
Q. And that's based on an embedded cost of debt as calculated and a proposed Rate of Return on equity of 9.75 percent, correct?
A. Yes, it is.
Q. Now, you're, I believe on record as saying that you feel that there's no range required to be set in conjunction with your proposal for the Rate of Return on Rate Bast as filed?

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A. At this point, Hydro has not requested a range to be set. It has filed the application based on the ROE of being nine and three quarters percent. And at this point, we'll be awaiting further direction as to what the results of this hearing will be.
Q. Does Hydro also recognize though that the policy in this jurisdiction is that a range on the Rate of Return is employed and that, in turn, is coupled with the definition of an excess earnings account?
A. I'm aware that this is what has been applied to Newfoundland Power, yes.
Q. Okay. And as I understand Hydro is suggesting that it should receive a Rate of return on this Rate Base, as a factor of a Rate of Return on its equity, similar to what was provided to Newfoundland Power in its most recent General Rate Application, correct?
A. Yes, Hydro is requesting that the--based on the assessment of risks for Hydro that had been done by our financial expert, Ms. McShane, that the assessment of the business risks that Hydro is subjected to are similar in nature to an investor owned utility similar

MR. ROBERTS:
to Newfoundland Power and that's the basis for the request.
Q. And Newfoundland Power is subject to a order that imposes a range on its approved Rate of Return on Rate Base, correct?
A. Yes, I believe you are correct, 50 basis points.
Q. So, wouldn't you agree that, I guess, in the case of Hydro, you should get the "fleas with the dog" as they say. That if you're going to get or apply for a Rate of Return similar to that of Newfoundland Power, that would entail also those additional and regulatory principles of ranges on that approved of Rate of Return and then coupled with that, the definition of the excess earnings account?
A. The Board does have that power and direction to establish a range both on the Return on Rate base as well as the ROE, the same as what they have done for Newfoundland Power. The only thing that may be different is the spread that would be there, whether or not it would be treated the same or not. So, just as a hypothetical, let's say in 2005 your Rate of

Return on Rate Base actuals are a full 100 basis points higher than 8.15 percent that's applied for and if approved, based on the 9.75 percent, would Hydro feel that it should not have to take that into account?
A. If the Board approves, as filed and doesn't provide a range, then from my perspective and I'm not a lawyer and I'm not prepared to go down that route, then I don't think there would be any option to Hydro, other than to advise the Board that we have exceeded what they have approved and seek guidance from the Board, either to do a refund or whatever may be directed by the Board at that point.
Q. Okay. So, what curiosity, in your financial projections for 2003 to 2007 is filed under CA-3 and if we go to roman numeral four first, no back a page, it was the executive summary that you had, yes, there you go. There's two provisions, I'll just draw them out first and then I'll get you to comment on them. It's the second bullet there. It says the years 2004 onward are projected to be test years meaning that rates will be adjusted annually to recover each year's cost. And then over on

page 13. It's headed rates, Mr. O'Reilly, no, one more page forward, there you go. The first paragraph there, Mr. Roberts, says this financial projection is prepared on the basis that 2004 through 2007 would be test years meaning there are annual rate adjustments. Detailed cost-of-service studies have not been completed for 2005 and beyond. However, rates have been estimated using Hydro's planning models that use simplifying assumption. Projected rates and rate changes are believed to be indicative based on the assumptions used, but not as precise as if detailed cost-of-service studies were available. Is the term test years being used in this document different than the sense of test year used for the regulatory process?
A. No, what we're saying there is that the test year would be exactly as we're doing now for 2004, that level of detail has not been done in this financial model.
Q. Yes. So, your rates--you're seeking approval for rates based on a certain rate of return and revenue requirement for 2004. So, that's your test year, 2004.

A. Yes, and this model is exactly that; it's a model that's at a very high level. It's not trying to design and do detailed cost-of-service studies and it's to be illustrative of what would happen, well, over time based on the assumptions that are applied here. And it's exactly that, the illustrative is the if costs were changing and you were to maintain your return on equity of 9.75 percent, here's what would theoretically happen over that period of time.
Q. Okay. But when it says, meaning there are annual rate adjustments, what does that mean? Does it mean that -
A. No. What the model has done is it has looked and it says, well, are you still holding, say, at your 9.75 percent. If you haven't, then your costs have changed. What is your new mill rate.
Q. Okay. Buy Hydro is not proposing as part of this application of forecast rate adjustments for 2005 and 2006 and so on?
A. No. This financial projection is exactly that, it's just a projection based on a bunch of assumptions.

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MR. KENNEDY:
Q. Okay.
A. And a requirement for other than that would require full-fledged hearings similar to what we're going through now. And the intention is not here to come back every year for a rate hearing.
Q. You're not masochists? (Laughter). Okay, I just wanted to turn to intercompany charges, if we could, Mr. Roberts. And the first place we'll start would be PUB-13, page 4 of--well, just look at the question first. This is, provide all studies, documents, data, so on and so on and calculating the total amount of cash working capital, inventory supplies, deferred charges.
A. Yes.
Q. Okay. If we could go to page 4 of 7, there we go. I just wanted to get the order of magnitude. So, we have a total operating expense for 2004 of ninety eight million eight twenty five, correct, ninety four eight twenty five?
A. Ninety four eight twenty five, yes.
Q. And then we've got CF(L)CO recoveries of one

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million seven seventy seven?
A. Yes.
Q. All right. And that represents 1.41 percent of your total operating expenditure, correct, your total cash -
A. Yes, I believe so.
Q. - outflow.
A. Yes.
Q. Now, one question before we move off of this exhibit, the "number of days" column, this is the numbers of days used in your Lead Lag Study, correct?
A. Yes.
Q. All right. And it's indicated that the CF(L)CO recovery has a 30-day allotment factor.
A. That's what is shown there, yes.
Q. All right. Now, as I understand it, the way that Hydro bills CF(L)CO for its intercompany charges is that it sets a budget for the year. In this case for 2004, $1,777,000.00, correct? That's the budget for 2004?
A. Yes, I'll accept.
Q. That's the budgeted cost recovery that you expect to obtain from CF(L)CO for 2004?

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A. Yes.
Q. All right. And then you break that down into twelve monthly allotments and you bill CF(L)CO on a monthly basis?
A. We would take the annual number and divide it by 12 and every month we would bill CF(L)CO the same amount for 12 months.
Q. And if there's an adjustment that needs to be made, it's made early in the next fiscal year?
A. If there is any adjustments, be it positive or negative, that the adjustment would be determined in January once actual results are known and the recalculations are done. And it would be paid in February together with its normal billing for the next year.
Q. And that adjustment for instance, if this was 2004, if that figure is accepted, that adjustment is made in early 2005, it gets booked in 2005, correct?
A. No, we try, if we can -
Q. To drag it back into 2004?
A. - to get it recorded into the year in which it happened.
Q. Okay.
A. So, for a financial statement purposes, we try

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to limit the amount of reconciliation that we had to do.
Q. Okay. Now, so the days that's indicated there, does that mean that Hydro is incurring those expenses on behalf of CF(L)CO and that it's 30 days later that Hydro gets paid for those expenses that were incurred. Is that what that 30 days means there?
A. No, the 30 days is trying to be representative of the types of costs that are up above. We actually bill CF(L)CO and then it's paid.
Q. Okay. So, let's just look at the insurance, for instance, it's minus 182 and a half days, so that would indicate that you prepay your insurance?
A. Yes, but within this calculation, there's no cost associated with CF(L)CO for insurance.
Q. No, no, I'm just using it for comparison purposes on your Lead Lag.
A. Yes.
Q. You prepay your insurance, so that on your Lead Lag, it's booked as a minus 182 and a half days, correct?
A. That's right, yes.
Q. On your Lead Lag for the CF(L)CO recoveries,

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MR. KENNEDY:
you've got it in so it's a 30-day lag, instead of 182 day lead.
A. Yes.
Q. All right. Now, any lag is what ends up creating the working cash allowance provision, isn't it?
A. Yes, that's one of the components.
Q. Okay. So, is it the case then in CF(L)CO's recoveries that Hydro--that there's a 30-day lag between why Hydro incurs the expense for CF(L)CO and when it actually gets paid by CF(L)CO for the work that was done?
A. Well, the billing is not based on when the costs are being incurred. It's based on the annual amount divided by 12. Whereas the salaries as an example, if you go up to that line, on an average of 12 days, but there's a portion of that that's going through for CF(L)CO.
Q. Okay. I'm still at a loss to know how the 30 days ended up in the Lead Lag study for the CF(L)CO recovery? Why is there a 30-day lag on the CF(L)CO in your Lead Lag study?
A. Well, the 30 days, I think, is just a normal

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representation of what a month would be as the amount of time for the costs and we bill them on the first of the month. So, we're actually giving them back a credit and reducing the weighted by the equivalent of 30 days. We had CF)L)Co.'s money on the first of the month and we had the use of it, so it's reducing what's up above.
Q. Okay. Can we go to NP-15, please, Mr. O'Reilly, if we could go to the next page, yeah. This provides just a summary of the cost recoveries from CF(L)CO, are you familiar with that exhibit, Mr. Roberts?
A. Yes, I am.
Q. Okay. One curiosity is there's a line item there, treasury and you've got treasury at 2004 at 0 dollars. Is my understanding correct that that's actually as a result of the organization that took place in Hydro commensurate with your becoming the CFO?
A. Yes, if you'll look on line six and seven, there were two components in three and in 2004, they've been combined into one.
Q. Okay.
A. What hasn't changed is the elimination of the

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two names because they're only effective in 2003. The new thing would be called the finance section.
Q. Okay. The CF(L)CO counter charge, number four, $20,000.00 billed back to, in effect, billed back to Hydro. What does that relate to?
A. That's an amount that's charged back to Hydro and reflected in the CF(L)CO administrative fee to cover the use of facilities at Churchill Falls by Hydro.
Q. So, Hydro uses facilities in Churchill Falls?
A. Yeah. We may, on occasion, utilize facilities at Churchill Falls and that's to reflect a charge for that.
Q. Now, Hydro owns 65.8 percent of CF(L)CO, correct?
A. Yes.
Q. The other shareholder is-
A. Hydro Quebec.
Q. - Hydro Quebec. Does Hydro Quebec also bill CF(L)CO for support of the nature as detailed in this NP-15?
A. No, it does not.
Q. Does it bill CF(L)CO for anything?

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A. I know CF(L)CO bills Hydro Quebec we do maintenance of various facilities that have been installed and there are agreements with Hydro Quebec where CF(L)CO will invoice those costs to Hydro Quebec. I'm just trying to go through the other company that I've got responsibility for and see charges--I'll be honest with you, if there are, it would be a very rare occasion that some would be billed back.
Q. Right.
A. Most times it's CF(L)CO billing Hydro Quebec.
Q. Now, there was mention that there is a contract between Newfoundland and Labrador Hydro and CF(L)CO concerning these cost recoveries, correct?
A. There is--on an annual basis, the Administrative Services Agreement would be reviewed--I should back up. Hydro will prepare a, the Administrative Services Agreement such as what you see here, and it would outline the cost and the various categories. That would be provided to the CF(L)CO Board of Directors for review and approval. And based on the results of that

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MR. ROBERTS:
review, then the agreement would be signed between Hydro and CF(L)CO saying that for the, say as an example, the 2003 year, the administrative costs are going to 1,795,000 and it would be signed by somebody to represent Hydro as well as somebody from CF(L)CO and then things would just proceed as normal.
Q. Okay. Now, the policy, if you will, of these recoveries for work performed by Hydro for CF(L)CO is one of recovering your costs, is that correct, as opposed to, for instance, charging a market rate for the work that's performed.
A. It's primarily based on cost plus any other appropriate costs or sharing or costs for each facility.
(11:45 a.m.)
Q. So, it's not based on market rates?
A. It's not based on market rates; it's based on costs plus allocations for other costs that would be utilized for CF(L)CO.
Q. Okay. And Grant Thornton have, in their report, provided, in their 2003 GRA report,

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provided some information about the policy and analysis of your approach on the recoveries. And you, yourself, in your exhibit JCR 2, the one we had out previously, the non-regulated operations, provide a description of how Hydro goes about recovering the costs incurred in relation to work performed for CF(L)CO, correct?
A. Yes.
Q. All right. I just wonder if we could just put it in concrete terms, let's deal with the management first. If you, as CFO, do work for CF(L)CO, you maintain, as I understand it, a time sheet.
A. Yes, I do weekly time sheets and in the case of time that I spend on CF(L)CO or other entities, I log that time and record it on a weekly basis.
Q. And then how does that time get converted to dollars for the purposes of the actual cost recover?
A. The hour that I worked on CF(L)CO is costed out to the payroll system and it's using my actual hourly rate that's put through and it's coded to, as we refer to it, as the work

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order. So, we have work orders established for the areas that are providing services to CF(L)CO. So, there would be a work order established for management, as an example, for which both myself and the remainder of the management team, as they provide services to CF(L)CO will complete weekly time sheets and that time would be recorded into that.
Q. Now, your actual hourly rate that you referred to, that is a combination of your salary, your benefits and what have you?
A. That would be my salary plus a loading for fringe benefits.
Q. And is that worked out on a 37-hour week then to get that hourly rate, do you know?
A. I'm going to say that the rate in my case is probably based on 1950 hours.
Q. That's a billing, sort of, related rate then?
A. Well, that would be a, I think it's a 37 1/2 hour week, it equates into 1950 hours for the years versus if you were an operations unit, it would be 2080 which is based on 40 hours a week.
Q. And so if you work two hours on a CF(L)CO related matter, it would be two over thirty

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seven and a half times your hourly rate.
A. Times whatever the hourly rate is based on 1950.
Q. Okay. Now, as I understand it from your description in JCR-2, there's also an add on to that figure for costs related to your executive assistants, is that correct?
A. Yes, executive assistants for management would be allocated based on the ratio that was developed from the executive management themselves. So that if--a combination of finance and production and TRO and Human Resources and legal and the president, if that worked out to be 15 percent for the year, then 15 percent of the costs associated for the executive assistants would also be charged to CF(L)CO.
Q. So, for instance, and I'm sure you do your time sheets in a timely manner, Mr. Wells, I'm guessing, my not be as diligent in performing paper work. I could be totally wrong, but his executive assistant, for instance, its assumed that person is also providing support for Mr. Wells to be able to provide his services to CF(L)CO and then that's why there's that cost

MR. KENNEDY:
recovery as well.
A. The executive assistant for Mr. Wells works for Mr. Wells as well as the Vice-President of Production. So that--and--versus the executive assistant that's--on other side, is for finance and TRO. And then we have an executive assistant that's looking after the Human Resources and legal side of things. Mr. Wells does do time sheets. He may not be doing them on a weekly basis, but he does get reminders from me (laughter) and I also get reminders from my staff because we continue to monitor the results of what's happening in the CF(L)CO and admin. fee and it's relatively easy to go into the work order and find out that all of a sudden there's been no charged in for two or three weeks. And the question then would be asked, how come, where are the time sheets? If there are no time to be charged, well that's fine, but it is monitored from that point of view. We may be a bit late in getting them done, but they are done.
Q. So, you work say two out of thirty seven and a half hours on a given week on CF(L)CO matters,

that ratio then gets applied to the executive assistant that supports you and their costs are added to your costs?
A. Their costs end up, at the end of the year being added to.
Q. Your engineering department, when they provide services to CF(L)CO, they too do so by the same method of using time sheets?
A. They would use time sheets as well to track the provision of engineering services.
Q. Now, are you aware that in the case of Newfoundland Power, that engineers that do work for non-regulated entities are billed out at a market rate or what's considered to be a market rate rather than a pure cost recovery? Are you aware of that?
A. I guess I only can recollect there was some discussion, as to what it was in connection with, I'll be honest with you, I wouldn't be able to say that I have any degree of familiarity with it whatsoever.
Q. Has Hydro ever considered charging market rates for its personnel like engineers or environmental services, ones that are readily determinable by looking to the market of what

that rate should be?
A. If, in the case of CF(L)CO, CF(L)CO also has its own engineering staff at site. So, the level of service that's being provided is not that significant and it's only to facilitate special requirements that's not being done at site. Have we looked at charging market rate out? The answer is no. We believe that the way that we're doing it now of using the time sheets, loading it with fringe benefits is utilizing, and charging--using that same ratio to allocate other costs, by the way, that's the other point that I should remember, is, you know, a fair reflection of the cost that should be removed from Hydro.
Q. Would you agree with me that there is an opportunity cost to Hydro by having its employees performing work for non-regulated entities?
A. There is an opportunity cost there because you may end up having some of our expertise used on non-regulated operations to a third party, as an example, but in doing that, it may entail the backfilling of that senior person. So, the amount of additional opportunity to

earn a margin or a profit on that transaction can be minimized.
Q. Well, I guess I was thinking opportunity costs in relation to, that if you've got your employees working for CF(L)CO, then they're not working for Hydro. And for instance, some efficiency gain that might have been achieved by that person, if they were fully dedicated to Hydro is lost and if that's an intangible that you're not recovering right now. That opportunity cost is to Hydro.
A. I guess when you look at the services that Hydro is providing, it's not a full-fledged individual that's being dedicated. It's part of me and it's a part of somebody else and whatever. And CF(L)CO does pay its share and full cost of what's incurred, even to the point of view of if an employee's position is terminated--well, I shouldn't say that. If an employee's position was made redundant and the employee was entitled to severance, then CF(L)CO would also pick up part of that severance costs. So to the extent that we can, CF(L)CO pays what we consider to be its appropriate share of all costs that are

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associated with having these employees, and these aren't fully dedicated employees to CF(L)CO. As I mentioned, these are parts and pieces of people that are being used to provide a service to CF(L)CO.
Q. Could we just go back to NP-15, please? Really there's three large items here, Mr. Roberts. There's the controller's department, 365,000. There's the IS&T figure of 525,000, and then there's materials management for 481,000. Now in the case of the IS&T department, that doesn't involve the use of time sheets or proxies for overhead, does it, the allocation of the recovery for your IS&T department? Could you explain how that's recovered?
A. In the case of IS&T, as you can appreciate in using a common system, it's difficult to say am I doing CF(L)CO today and Hydro tomorrow and whatever. If there happens to be a particular issue that gets addressed, then we're using a common system, it's a common issue, just who discovered the problem first. What's been used as a basis to allocate the

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IS&T costs to CF(L)CO is it's being based on the number of computers that exist, that CF(L)CO have of the total that are in the Hydro Group. So the ratio of the total of personal computers, if there's 600 in the whole group and CF(L)CO has 200 of them, well, it's two over six times the IS&T costs is what's allocated to CF(L)CO.
Q. So why would the IS&T be treated that way instead of requiring your IS&T employees to track their time with time sheets in the same manner as the other positions?
A. Because, as I just mentioned, if there's a phone call tomorrow that comes from an employee of CF(L)CO that says "I've got a problem here in the maintenance module," well, the problem is common to both companies. If there's something wrong--Hydro is using the exact same model. It's just somebody at CF(L)CO may have found it before an employee in Hydro found it. So it's a common set of software and it's a common fix that's of benefit to both. So if the issue was identified and a CF(L)CO employee happened to find the issue and IS&T rectified it, then

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it's rectified for both companies because we're both using the same software.
Q. Sure. And that's the assumption that -
A. And that's the assumption.
Q. - that if there's an issue that arises, it's common to both of you?
A. It's common to both.
Q. But that wouldn't always be the case, would it? As you said, if there's 200 computers being run by CF(L)CO, you would have your own--CF(L)CO would have its own servers. It would have its own networking. So it -
A. It owns its own servers and it does have some support within its own organization, but for the main systems of like our JD Edwards system, our Lotus Notes applications, those common systems that are to all, this is how the allocation of the costs would be done.
(12:00 p.m.)
Q. Some are common; some are not?
A. Some are; some are not, and like for instance, CF(L)CO has support people, as you're saying with the local servers at site, but the main crutch of the issue would be through Hydro Place and the support that's available there.

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It would be limited.
Q. You run the JD system, as I understand it, Hydro does?
A. Yes.
Q. And CF(L)CO uses the JD Enterprise system -
A. Yes.
Q. - for some of its financial planning and modelling?
A. For all of it. The only thing that CF(L)CO doesn't use is the UCIS customer billing system. But all other modules, they're jointly used.
Q. And the materials management figure, that's treated the same way as your controller's department, in that the cost is tracked through the use of time sheets?
A. In the case of materials management, what you're looking at here, this would be the cost associated with Hydro Place and the provision of services for our library and our office services, and the methodology that we're using there is that we come up with what we call and equivalent complement basis, and what that entails is we look through the employees within Hydro Place, arrive at a total number

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of positions and then, based on the analysis that would be coming from management, as an example, the ratio may turn around and say it's .3 of a position is associated with that. If you go into the controller's department, it may be the equivalent of three and a half positions. So we total all those up and that as the percentage of the total positions in Hydro Place is how we would allocate the common costs for like the mail room and the billing costs associated with CF(L)CO, that are being provided to CF(L)CO on behalf of Hydro.
Q. In the case of your controller's department and the time sheet based recoveries that are used, there's the description--if we could just go to JCR-2, Mr. O'Reilly, and page 7, yes, controller, just put that full--there's a description here, Mr. Roberts, of what actually is provided by the controller.
A. That's correct.
Q. The most significant accounting services provide included in recording of actual costs in the general ledger, accounts payable,

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accounts receivable, processing, account reconciliation, financial and capital reporting, so on, reviewing capital and operating budgets, providing advice and assistance to CF(L)CO on the use and maintenance of the various JDE systems modules, federal and provincial tax, calculation of preferred dividends, and preparing various reports for shareholders.
A. That's correct.
Q. Would you agree with me that if you needed to, you could go to the market, the open market, and hire someone on a contractual basis to provide those kinds of services? In other words, if Hydro wasn't providing those services to CF(L)CO, CF(L)CO would either hire someone to do it themselves, or they would in turn hire an accounting firm or some sort of consultant to provide that kind of work?
A. The services could certainly be provided by somebody outside of Hydro. The question is at what costs.
Q. Correct. Likely to be higher than the cost that you're recovering right now? A consultant would charge more, wouldn't they?

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A. Consultant would certainly charge more because he's going to build in a higher recovery and an element of profit within their particular billing based on what their predetermined billing rates would be.
Q. And I take it that you don't feel that's appropriate for Hydro to do in these circumstances?
A. Personally I think the methodology that we're using meets the description of being a fair allocation of costs to CF(L)CO for the services that are being provided.
Q. Okay. Just two snappers. One is the--you've referenced actually earlier today the cap that Hydro has imposed on it by Order in Council for promissory notes.
A. Oh, the 300 million.
Q. 300 million. And that is, as you said, by Order in Council, correct?
A. To the best of my knowledge, yes.
Q. So that's government imposing a limit on Hydro's short-term borrowing ability?
A. Yes. It's by Order in Council it's limited the amount that can be financed in short-term.
Q. Do you have any other mechanism other than

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through these promissory notes as limited by the Order in Council to 300 million to avail of short-term borrowings?
A. I don't believe there is because you have to recognize now in the 300 million all of this is guaranteed by the province, so both our long-term debt and our short-term debt is guaranteed by the province. Whether or not somebody else would be prepared to loan us money without a guarantee and whether or not that would be in contravention of this cap that's imposed by government, I really haven't investigated in any way.
Q. Does, in your opinion, the $300 million cap provide less flexibility than you would otherwise like to have as CFO of Hydro? In other words have there, for instance, in the last short while in particular where the short-term interest rates have been as low as they have been times when you wish you could have availed of greater short-term borrowings to take advantage of that but were unable to because of the $300 million cap?
A. That's a difficult question because what you have to do is you have to keep balancing the

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ratio of what you have in long-term debt against short-term debt. And you're trying to find, and there's no magic numbers that it's got to be 75/25 or 80/20 or 85/15. It's, you know, exercising judgment and information that's available to the time. You don't want to catch yourself in the position where you've got a significant amount of your debt outstanding in the short-term rates and all of a sudden the market can turn around on you and you could get caught the other way. So, it's a balancing act of what you feel is a reasonable allocation between short and long-term. We do, through that exercise, do consult with our financial advisors. We do have some information that's available relative to those ratios that are exercised by other utilities and we use that as a guide in us determining where do we feel comfortable in the ratio of long-term and short-term.
Q. That's all the questions I have, Chair. Thank you, Mr. Roberts.
CHAIRMAN:
Q. Thank you, Mr. Kennedy. Thank you, Mr. Roberts. Ms. Greene, do you have some redirect?

GREENE. Q.C.:
Q. Yes. Thank you, Mr. Chair. I have some limited redirect, and as well, we will be in a position to respond to the two undertakings that were given yesterday at this point. The first question that I have for you in redirect, Mr. Roberts, arises from questioning of Mr. Kelly on October 14th. And I wonder, Mr. O'Reilly, if you could bring up the transcript of October 14th at page 135? And you see there, there was discussion with respect to the fuel conversion factor at Holyrood and what time impact would be on Hydro if the actual fuel conversion factor at Holyrood was higher than had been set in the test year. And you'll see there is a question at the bottom of page 135, we're beginning at line 23, Mr. Kelly said, "If Hydro had--if everything else had panned through exactly as tested and all that had changed was the fuel conversion factor, that $6 million would have gone right to Hydro's bottom line, wouldn't it? Would you agree with that?" And your answer was, "I'll have to think about it, but I think you may be right." And I'd like you now to address that question and what is the impact if there is improvement in the fuel conversion factor?

A. Yes. The answer that I gave is not correct, and that's why I wanted to think about it, because I knew there was something that was sticking in my mind. Actually, IC-371, in response to that the question was asked in relative to a follow-up on IC-207. The change in deficiency had been quantified to be approximately a $6.1 million savings. But of that efficiency $2.4 million would be a savings to the rate stabilization plan and only 3.6 would impact on Hydro's bottom line.
Q. So with respect to the improvement in the fuel conversion factor being better than included in the test year revenue requirement while there is an impact on Hydro's bottom line, it's not the full impact of the improvement, is that correct?
A. No, it's not. There would be some savings that would be attributable to the Rate Stabilization Plan as well.

Q. And the response to IC-371 is an illustration of how it worked with respect to a specific savings, is that correct?
A. Yes. This one reflects the savings that are associated to the RSP and the difference between the 2.4 and 6.1 is the impact on Hydro's bottom line.
Q. The next question that I have on redirect also arises from cross-examination with Mr. Kelly when he was discussing with you some of the reductions in staffing that has occurred at Hydro. And he left the impression in his questioning that the operating departments may have had more of a reduction in staffing, and he took you to only those departments. And I'd like to take you to the others. So if we could, please, go to MP-9? Here Mr. Roberts is whereby each division the change in complement from '97 has been outlined. And for ease of convenience I'm going to start with 1999, because if you look through, you'll see that there was an increase from 1998 to 1999 in production. It went up from 278 to 320. What happened in that from '98, sorry, to '99?

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MR. ROBERTS:
A. Well, in 1999 the former Management Information Systems or the computer side of operations was combined with the tele-control aspect of production and that was transferred as of January the 1st, 1999. Those two departments were amalgamated into one.
Q. So if we looked over to the finance division, we should see a corresponding decrease in 1999, is that correct, because that MIS staff had been included in that complement up to the then?
A. Yes. MIS were included in finance up to the end of 1988--1998.
Q. So for comparison purposes with the new structure with the MIS change I'd like you, looking at production, what has been the change in complement from 1999 to August, 2003?
A. Well, in the case of the IS and T--IS and T-- in the production division at the end of 1999 the complement was 320, at August '03 it's now forecast to be at 301. There's a reduction of 19 positions which represents six percent.
Q. Go to the next page, please, Mr. O'Reilly?

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And here's the human resources division. And for the time frame 1999 to 2003 what has been the reduction in complement in that division?
A. Well, there's a reduction of 12 positions which represent 17 percent.
Q. Next screen, please, Mr. O'Reilly. This is transmission and rural operations. Again, for the period for 1999 to August, 2003, what has been the reduction in complement in that division?
A. Yes. There's a reduction of 70 positions and that translates into 17 percent.
Q. The next page, Mr. O'Reilly, is finance. Again, could you please advise what the reduction has been from 1999 to August, 2003?
A. Yes. There's been a reduction in ten positions and that equates to a 12 percent reduction.
Q. And there you can see the drop from 1998 to 1999 reflects the transfer of the MIS department to production that we just talked about, is that correct?
A. Yes, it is.
Q. The next page should just be the executive management internal audit and corporate

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communications. What has happened here?
A. On this page we can see that the overall change for the Company as a total has gone from 901 down to 791, and that's a change of, I believe it's 12 percent I've got marked here, if I can read my own writing.
(12:15 p.m.)
Q. Now, following up on this point Mr. Kelly then took you to IC-39, which I'd like to go to as well. And I'd like to look at page 3, where again he compared certain actual salary costs starting in 1997 to forecast costs for 2004 and he threw out a lot of percentage increases. And what I would like to talk to you about is the couple of the ones he didn't talk to you about, the first one being human resources. The increase from '97 or the actuals is 5.5 million to the forecast of 2004 of 11 million where Mr. Kelly pointed out that was more than 100 percent increase. And you started to explain and I guess you didn't--as Mr. Kelly didn't pursue the questioning with you as to the reason for that from actual '97 to forecast 2004. What is the reason for that?

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A. Well, included in the 2004 number of 11095 are some corporate costs. One in particular is the employee future benefits. There's $3. 7 million included in the 2004 number that is not included in either '97 or '98. In addition to that there's an increase in the group insurance costs of approximately $800,000 between 1997 and 2004. And the other item that's contributing to the difference is that in the case of apprentices, apprentices are budgeted for in the human resources and legal division because over the period of time they're moved from division to division and location to location depending on the requirements and where their rotations are. And from a budgeting perspective, they are controlled and monitored through the human resources and legal division. And there was an increase in the number of apprentices that are in the system in 2003 and in four relative to what was there in 1997.
Q. So if we look at the footnote that was there by human resource and legal, it indicates, and I take from your answer that the reason for the increase are corporate costs related to

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GREENE, Q.C.:
all of the divisions such as employee future benefits for all employees and group insurance for all employees and are not strictly related to just this human resources division?
A. That's correct, they are total Company costs.
Q. The next question that I have on redirect arises from the cross-examination of Mr. Seviour yesterday. And in response to a question, if we go, Mr. O'Reilly, please, to page 112 of the transcript of October 15th, page 112? And I'd--there on line, starting at line 2 and going on to line 3 you stated that, "One of Hydro's Board members is the Deputy Minister of Finance." Is that correct?
A. No, it's not. The actual appointment is the Deputy Minister of Mines and Energy, not Deputy Minister of Finance.
Q. The last question I have for you on redirect also arose in the cross-examination of Mr. Seviour. And if we could go, please, to the transcript also of yesterday, page 138? And there beginning at line 21 Mr. Seviour asked you a question and he asked you about Hydro's position with respect to being treated as an

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investor owned utility, does that continue to be the case. And you responded yes. And I wanted you to explain what you meant by your one word answer there?
A. Yes. My reference was there is that in the determination of the return that the utility is seeking is based on the assessments of the risks of the utility and the assessment of those risks by our financial expert, Mr. McShane, has concluded that the business risks that Hydro faces are similar to an investor owned utility such and Newfoundland Power. And based on that assessment and that conclusion, then the return should be similar to what would be received by an investor owned utility.
Q. So Hydro's position with respect to being treated as an investor owned utility relates to the rate of return, is that correct?
A. Yes, it relates to the assessment of the rate of return that should be received based on the risks that the equity holder is subjected to.
Q. That concludes the questions I have for redirect. I'd like now to turn to the response to the two undertakings that were

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provided yesterday. The first was an undertaking provided to Mr. Kelly. And if you go to the transcript, Mr. O'Reilly, beginning at page 69? You'll see there the start of the discussion with respect to the reduction in the temporary employees in 2003. And the specific undertaking is provided or asked for beginning at line 21. And at line 22 the undertaking was, "What is the savings, what is the value of the reduction in the temporary employees from 2002, 194, to the 2003 number of 131?" First, before we get to the answer I'd like you to comment on the reference of the reduction from 194 to 131. Do you agree that is a correct statement of the reflection of the temporaries for 2003?
A. No, it is not. The 194 represents a number as of the end of 2002 and the number of 131 that's reflected for 2003 is the full-time equivalents that are anticipated in 2003. So the numbers are not comparable.
Q. However, there was a reduction in temporary wages, is that correct, in 2003 over 2002?
A. Yes, there is a reduction in the temporary wages from two to three, and that's in the

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order of approximately 1.6 to 1.7 million dollars.
Q. A second undertaking was provided, as well, to Mr. Kelly and it is on page 75, starting on page 75 of the transcript, and it relates to professional services. And you'll see beginning at the bottom of page 75, going over to the top of page 76 Mr. Kelly asked you to provide--and I'll go to the top of page 76 there. It's actually beginning in line 1 at the end. He asked, "Can you give the Board any sense of what makes up that other approximately $900,000?" And, Mr. Roberts, that referred to professional services in 2002 where Grant Thornton in its report had summarized the main categories of professional services but had not given a total accounting, leaving approximately $900,000. At this time could you outline for the Board what are the categories of professional services in that $900,000 as Mr. Kelly asked you to do?
A. Yes. What Grant Thornton had outlined in their report was just representative samples of some of the professional service costs that they had actually hauled (phonetic) the

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MR. ROBERTS:
vouchers on and confirmed as to what the costs were. In addition to that, there are additional costs and I'll just go through some examples that I have here for you. The cost of our annual report and our environmental report has not been reflected in the analysis done by Grant Thornton, that approximately $78,000.00, some work with insurance claims is $6,000.00, some costs and treasury related to our banking services, fee for Dominion Bond Rating Services and tele-rate which gives us information relative to rates, there's $80,000.00 there for that. Customer services, our customer service survey that was done is $28,000.00. There were some costs in rates relative to our report on all hedging and other costs of service related matters for 44,000. There were some costs in our economic analysis section relative to economic forecasts and the fee paid to PERA (phonetic) for the forecasting on the number 6 fuel oil for 44,000. There were some costs for arbitration, $11,000.00. There was $224,000.00 for additional information

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technology items covering assistants that were required relative to our intranet document management security. There was $141,000.00 associated with Holyrood and that included such things as utilization of services of a chemical consultant, some assistants on land fill and water analysis and some current tests that had to be done on unit number one. There are also, from the generation side of things, the cost of the Annual Dyke Board visit for $38,000.00. There were also some things there from an environmental nature for $83,000.00. So, that gives you the idea of the types of things that are making up the $900,000.00.
Q. Thanks, Mr. Roberts, that concludes both the re-direct and the response to the undertakings given yesterday.
CHAIRMAN:
Q. Thank you, Ms. Greene. Mr. Kelly, are there any follow-up just on those two specific items?
KELLY, Q.C.:
Q. No, Mr. Chairman, not at this time.
CHAIRMAN:
Q. All right, thank you. We move to Board

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questions. Commissioner Saunders?
COMMISSIONER SAUNDERS:
Q. Yes, just a couple, Mr. Chair. Mr. Roberts, throughout your evidence, not only your evidence, but the evidence of the Company, the pre-filed evidence particularly I'm referring to, with no specific reference, but you use the words "staff complement" and you also talk about FTE's. Would you explain for the record what the difference is in terms of its relationship in each case to budget and actual costs?
A. The reference to staff complement used to be in equivalent to full time positions permanently approved.
Q. Not necessarily filled.
A. Not necessarily filled. There could be vacancies, but our full-time complement would reflect, as we just said, filled and unfilled at that particular time, but it was an improved complement position on a full-time basis. In the case of the FTE's, you've now converted, Fulltime Equivalent, those full-time positions and you've now taken all your temporary hours and based on whether or not

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it's an employee that's working 1950 hours or 2080 hours a year, we've done the math, convert those hours into the equivalent number of people, that combined with the what was referred to as the permanent complement will equate and give you the number of Fulltime Equivalents.
Q. Okay. Why do you continue to use both?
A. Well, in history, and it's old habits that are hard to break, but a lot of our historical information only tracked information by fulltime Equivalents. And in the case of the temporaries, on a historical basis, all we had was the number at a point in time. So that, for instance, as of the 1st of June, you could have started off with 100 temporaries, but by the end of June, you're geared up for your maintenance season, the number could increase to 300. But in the new way of things, of doing it, looking at the Fulltime Equivalents, that eliminates having to worry about that comparison.
Q. Are you making the transition to FTE's, is that in the process?
A. That's already in process and it started the

MR. ROBERTS:
1st of 2003. There will be growing pains in trying to get used to the change because you're moving away from looking at things on a dollar basis to, now where it should be, is on an hourly basis. What hours do you need to do the work, rather than before you were block of dollars and you were trying to get the work to be done. So, I think in the long term, it should be more beneficial to us.
Q. So, some time down the road, we'll see the complement disappear from the -
A. The complement should disappear, maybe at the next hearing.
Q. All right. A question in relation to the credit rating of Hydro and the Province. And if I recall the dates and numbers, I think Hydro's debt equity ratio was declined from seventy eight twenty two to roughly eighty six fourteen over the past seven years or five years, from '98 to now. Would that be -
A. That sounds fairly close. I know it's approximately about eighty six fourteen right now.
Q. Right.

A. And it was, I think, below the eight twenty at an earlier date than in -
Q. Yes, it was, and I picked that up somewhere and I forget where it was.
A. I think it's in the report that's attached to Mr. Wells' evidence on the capital structure and the dividends. I may have given the history back in there through the capital structure.
Q. What has happened to Hydro's credit rating during the same period? Has there been any change?
A. No, because we are assigned the same rating as the province, but what continues to be outlined in the reports that are done by the credit rating agencies is that they still consider Hydro to be self-sustaining. And therefore, when they do the assessment and they look at the Province, they look at Hydro and say, yes, this company is self-sustaining and is not impairing on the Province. So, as long as that continues, we're comfortable that it won't impact on the rating that they will assign to the Province.
Q. What's happened to the provincial credit

rating over that same period?
A. Actually, I think somebody just changed because there's three rating agencies.
Q. Yes.
A. There's Dominion Bond Rating Services, there's Moody's and there's Standard and Poors. And I think recently, it may be Moody's, I think just changed the Province, it may have been like A- to A, but the ratings are all different between the three. They may all translate -
Q. Well, I'll put the question another way, has there been any deterioration in the Province's credit rating in the past seven or eight years?
A. I don't know if I could answer that question for you.
Q. Maybe you could find out.
A. Actually, if you would just bear with me for one second, Mr. Saunders.
Q. Sure.
A. I knew where the credit ratings were filed, they may indicate as to how long that rating was in effect. I'm looking, there was in NP-104 and I'm just looking at one of the ratings

that's here and it's one that I referred to yesterday. This is NP-104, attachment G with is DBRS. And as we track the rating of the Province, they do show the rating history and it shows 1996 was DDD low and as of 2002, it's BBB. So, I'm assuming that was an improvement.
Q. Sounds like it.
A. Now, the same thing--I don't know about the other ones, but the information is, the current ratings, and whether or not the other ones provide the same level of history, that, I'm not sure. But I know in the case of DBRS, they do provide a history of the ratings and what would be there for Hydro is also there for the Province.
(12:32 a.m.)
Q. Sounds like it.
A. Now the same thing, I don't know about the other ones, but the information is current ratings and whether or not the other ones provide the same level of history; that, I'm not sure. But I know in the case of DBRS, they do provide the history of the ratings and what would be there for Hydro was also there

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for the Province.
Q. It's probably on the record, I just thought you might have had the information readily available.
GREENE, Q.C.:
Q. If it's helpful, Commissioner Saunders, I can confirm there has been no deterioration in the Province's credit rating in the time frame you've referred to.
COMMISSIONER SAUNDERS:
Q. Okay, thank you, Ms. Greene. Okay, Mr. Roberts, I think I asked this question of Mr. Wells when he was on the stand, I'm not certain, but I know I had intended to, and that is, your contracting out costs, where do they show up? If I asked Mr. Wells, I didn't note his answer.
A. I'm trying to formulate in my mind how I can explain contracting out. We are limited in what we can contract out by our union contracts.
Q. Yes, I realize that.
A. There are certain services that we may require that aren't provided today by our union

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employees, and I'll use the example of IS&T, if we need additional resources, then that would probably come through professional services based on a project. We would engage Xwave or somebody like that or JD Edwards, for that matter, to provide that level of service that is not existing in house and it would be part of the work that would be performed by bargaining unit members. So it would be a function of what was being required would dictate where it would be recorded.
Q. Uh-hm. So where do you show your contracting out costs in various headings?
A. It would be in various expenditure categories or various projects. We don't try to -
Q. You don't track it.
A. We don't track it that way. We track by a project or by the requirement for the service and then that would dictate as to where we record it.
Q. You're carrying inventory normally, and I looked back over the figures of shop supplies, I think you called them, somewhere around 17 to 22 million dollars over the past several years. And there's been write offs

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approximating a half a million dollars, I say approximating within two hundred thousand of five hundred; in other words, between 300 and 700,000 of write offs. That inventory is located in several locations around the Province and Labrador.
A. Yes, it is.
Q. And you talked earlier in your discussions with counsel earlier this morning about the process you have in place in terms of verifying assets and so on, and I'm wondering if your store's inventory is included in that process?
A. Yes, that one has already actually started, actually in 2001, the initial started from the point of view of reviewing the inventory levels, but also what was in the inventory and is it still used and useful, should it be disposed of, is it surplus to what we really require to be carried if it's available down the street, then our inventory levels should be reduced. One of the initials that's described in, I think it's Section 9 of my evidence about the continuous improvements that we're doing, one of those represents the

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goods and services process. And what that process entails is that the responsibility for all the inventory has been put underneath the control of the materials/management section, which is underneath Ms. Greene's or in vice-president of Human Resources and general counsel. So the responsibility for all the inventory will rest in one area, and it's an ongoing process now of reviewing, continuously reviewing our inventory levels and continuing--we've always done in the past, we've always done spot checks of inventories and verified what was on the records, versus what was in the bins. But we're--and I guess you can say we're continuing now, in this process, to review with the areas, number one, the level; and number two, what's actually in inventory, towards reducing the amount of inventory that we have to carry. And as I mentioned in that regard, what we're looking at is in the particular areas, are there suppliers for which we're obtaining these parts from and if so, then why would we need to carry it in inventory and the supplier carry it, if it's readily accessible by going up to the street.

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MR. ROBERTS:
It may mean making arrangements for an off hour's situation, if we get into it, or maybe it means rather than carrying 20 items in inventory, we can carry 2 because the next day it's available there. So those things are being done on a location-by-location basis as well. And of course, the other thing is when you look at what's in inventory, sometimes in the electronics components, they can become obsolete relatively quickly and your spares have no value if you change your components.
Q. Yes.
A. But, you know, you were forced at one point to have some of these things on hand.
Q. Okay, thank you. I think those are all the questions I had, Mr. Chair.
CHAIRMAN:
Q. Thank you, Commissioner Saunders. Commissioner Whalen?
COMMISSIONER WHALEN:
Q. Good afternoon, Mr. Roberts. I just have one question and we can't see each other, but that's fine. And it relates to the method that Hydro uses for capitalizing the expenses,

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and it's really a follow-up question from P.U.7. I wonder, Mr. O'Reilly, if you could put up page 76 of P.U.7. That's fine there. And this was dealt with fairly extensively in the last hearing. Has there been any changes in Hydro's methodology for capitalizing expenses since the last hearing?
A. No, there has not.
Q. Okay. And at the last hearing, it was--and, of course, you would be aware, it was pointed out that Newfoundland Power does use a different method, I understand, or do you understand that to be -
A. Yes, I believe they do.
Q. And that method was the subject of a full review by Newfoundland Power by Order of the Board and the Board has approved that method, it's an incremental method, I think, of allocating capital expenditures.
A. Uh-hm.
Q. The Board makes the statement on page 77, "The Board feels that a review of the methodology approach used by Hydro to determine capitalized expenses will be appropriate at some time in the future." Does Hydro have a

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position on whether or not such a study is necessary or should be undertaken, of if this is an appropriate time to undertake such a study?
A. I'll be honest, at this point there hasn't been, with all the rest of the items that are ongoing for the hearing, there hasn't been much discussion taken place as to whether or not there would be anything to be gained from a further review. And I guess that's the best comment that I can make at this point for you, Commissioner.
Q. And this kind of a study is, my impression is that it's a fairly extensive and comprehensive--it wouldn't be a small piece of work, is that a -
A. It would require a very detailed understanding of the operation and it would take some time in which to complete. And it is, I guess, as I say, amongst other things, there are always going to be different methods and differing opinions as to how things should be done and what are the basis to arrive at it. The way that Hydro is doing it now is utilizing its time sheet and loading it for fringes and then

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marking it up by an overhead to provide what it feels as being a reasonable approximation of a charge out for the costs that are associated with that capital project. And it does make an allowance for the other people that aren't specifically developed--involved in a capital project, but do provide services and I think the rate that we're using presently is 6 percent. So, whether or not a study would actually entail having significant changes to that, I guess until you spent the time and the money to do it, you'd never know, but I think in my opinion at this point, that at least what we are doing is a reasonable approximation of being a fair and reasonable cost that's charged to our capital program.
Q. You haven't, internally, looked at the impact in terms of whether Hydro was using incremental -
A. No, we have not at this point.
Q. Okay, thank you, Mr. Roberts, very much. That's all I have, Chair.
CHAIRMAN:
Q. Thank you, Commissioner Whalen. Mr. Roberts, thank you very much for your testimony over

CHAIRMAN:
the last three days. None of us, I think up here, are professional accountants in any way, shape or form and I found, in particular, your explanations and the manner in which you delivered your testimony useful. Thank you very much.
A. Thank you.
Q. I have just a couple of questions. One relates to the business improvement strategy and I guess there's a little bit of a mystery in the sense that there doesn't seem to be very much in the way of paper attached to the study or implementation of that strategy, and indeed, in terms of looking forward down the road to what that strategy might employ by way of efficiencies and savings. It's very difficult, from I understand your testimony and Mr. Wells, to sort of predict that and indeed will be encompassed within the overall efficiencies and the productivity of the organization. And I guess there are hundred-- somebody mentioned 150 business units. I think you confirmed that and I think that was the number that I heard the last time and I

would think that within each of these business units there would be multiple processes, I would think, is that a fair statement?
A. Maybe I should try to provide a little bit of information to you. We refer to "business units", really in effect is what they are, are cost centers. For instance, we would have all our salary and labour costs in what we refer to as a Labour Business Unit. And a supervisor or a manager or director, could have responsibility for multiple business units, for instance, he could have responsibility for the labour, as well as some of the assets or the service structures that we have created. So it's not a supervisor for every single business unit or a manager for every single business unit. There would be multiples that would be associated to a director or a manager. But they are primarily cost tracking centers, very similar to the old methodology of the budget, but you just divorce the labour from work that was going on relative to our equipment. The processes that we're reviewing were cut across all lines, for instance, the review of the goods and services

process that I just briefly touched on with Mr. Saunders, would impact the TRO, would impact production, it would impact materials/management, so the change in the review of that process was looking at it on a company-wide basis and it will have impacts and ratifications throughout all the areas of the Corporation. It will entail, in some cases, a change to the way that we do things, for instance, the other one that I had described in my evidence is how we computerized our travel costs and virtually eliminated the processing of a travel claim. What that did within an individual business unit, it will change the way that people now start to budget for costs. They were budgeting for training, as being distinct that you include your full travel cost associated with the training. Now we've computerized and automated those cost, now the switch, so that what was in training now, will probably may only be the outright tuition fees, I'll refer to it, for the cost of the training. That was a decision that was made that it's more cost effective to have these things automated, if

you made the approval in the first place to do it, then if there's a way to automate the recording of the transactions, then we should be doing that. And we do have built-in checks in the case of the automation of the costs that are recorded on the purchasing card on a monthly basis. There is a selection criteria done of a representative sample of the number of credit card statements and notification is sent, and it could be sent to me, saying kindly review one of my director's statements this month, and I would do that detailed review and sign off on it. So even though we've automated the process, we have still built in some checks and balances to make sure that it's working as intended and that the costs are appropriate. And the impact of that would cut across all business units. And most of these processes that we're doing the view on, will do exactly that, the Goods & Services tax, Goods & Services structure that we're looking at and the consolidation of the control over the inventory, will impact what's happening in all of these various business units. The review of the way that we budget

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MR. ROBERTS:
work and we execute work will impact what's happening within these particular business units. The link that we're establishing now between actual financial records and equipment records and building that link will then facilitate better information for the field and replacement of assets, but it will also be a great facilitator to the preparation of the cost of service, because hopefully at the end of the day, the amount of reallocation of costs can be minimized. You'll never eliminate it a hundred percent, but at least it can help minimize the way that some of the costs now have to be allocated.
(12:49 p.m.)
Q. So these business improvements that you're talking about, the strategy is based on processes that cut across various -
A. To cut across the whole organization as a whole.
Q. Because inherently it's -
A. Now you may still find within various sections, like for instance the Meter Reader Route Optimization Study, which was a review

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that was on and was carried as well, you know, that was unique and wouldn't cut across, you know, the full Company line.
Q. I guess my question arises from the fact there would seem to me, by virtue of the fact that you're tracking costs, you're tracking labour, you're tracking materials within a business unit, that there are processes that occur within--and may be multiple processes that occur within a business unit, because ultimately the costs are attributed to work that's getting done. And there may very well be a combination of business processes that cut across units, I have no doubt about that. I guess my question surrounds the fact that again, there seems to be all kinds of combinations and permutations of processes that would be in place within Hydro. And is there, I mean, where do you go next with this business improvement systems? There must be some document, some report, there must be certain processes that you're looking at and the processes that you're going to look at in 2003, 2004, 2005, that has to be identified somewhere, does it not?

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A. Well, as Mr. Wells mentioned, he wanted the process kick started because of the circumstances that we're into. And the first area that was looked at, of course, was the accounts payable purchasing, arising from that, there were other processes identified and they were the ones that we're now working on. And I think as we move forward, there will be other ones that we know they're there, it's just that somebody has got to identify what's going to be the next one that we will tackle. If you look back, when we implemented JD Edwards, normally if you had all kinds of time on your hands and weren't under the gun with a Y2K situation, and what you would have done is you would have looked at your processes as you were doing an implementation, so that you would define your process and then the implementation would have been done. So really what we're doing now is we're utilizing the technology we have and doing the review of the process and see now how does it be fine tuned to gain the efficiencies that we can achieve by redesigning our processes. And there's not a master list of the processes

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that are yet to go, they will evolve as we get close to finishing and as people say, well, maybe the next process we should look at is the way that we bill our customers.
Q. So how does that evolve and what criteria do you apply in order to -
A. Well, right now, the whole process is headed up by, I'll use Mr. Wells' outline, one of our senior directors in the organization and he's been charged with the responsibility to manage and to roll forward this process. And one of the items that he will be doing will be identifying potential next processes that we should start to do the review on, and then that would come forward to management for a discussion and review, and there may be additional items that even I may raise within, say, look, here's an area that I think should be considered. But there's no master list prepared to date of saying, you know, here's fifty-odd processes. I appreciate it seems sort of ad hoc, but we're taking our time and trying to learn as much as we can in the two or three that we are doing.
Q. So that person comes forward with a list then

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CHAIRMAN:
and is it tied into the budget process then?
A. So he would come forward with a listing and then we would look at that from what's feasible and what can be possibly carried out in the time frame and what do you see as being the anticipated changes that can be done, and are they related to just one area of the operation, or as we mentioned are they cutting across all functional lines? Because some of these processes won't be cutting across all lines, they may be distinct to one particular area, as I mentioned in the Meter Reader Route Optimization Study, you know, that would be distinct to that section. And there may be other processes that we'll review that may only have implications to, say, production, may not apply to TRO.
Q. Who in the organization is responsible for that, the business and systems planning improvements?
A. Right now, we have a senior director, used to be the former director of TRO, reporting to the vice-president.
Q. Which vice-president?

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A. Well he used to report to Mr. Reeves, and in 2002 when we started this process, he was asked to undertake the role as heading up the process review initiative. And he is still responsible for heading it up and reports directly to Mr. Wells.
Q. I see. Can you just help me in this area a little bit. I heard you, again, I'm not a professional accountant, a professional finance person in any way, shape or form, I heard you say and I could refer to it in the transcript, but I thought the RSP in terms of, you said, I think, it's assigned the weighted average cost of capital, in terms of its costing?
A. Yes.
Q. Which would consist of debt and equity. Now when you describe that, again in the transcript that I read, you kept referring to promissory notes and I would have thought that would be debt which would somewhat cheaper. I don't quite understand how equity is applied--cost of equity is applied to the RSP, which would seem to me to apply then a higher rate, versus the cost of debt and that would--I

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don't know what the numbers would be, but that would be carried through, I would think, to the revenue requirement?
A. See if this will try to help you. If you look at Hydro's capital structure, any of its assets are financed through a combination of debt and equity. And debt is both long term and short term and short term being the promissory notes. So in the calculation of what the weighted average cost of capital is, it recognizes that the particular asset that you may have, part of it is financed through debt and part of it is financed through equity. It's treated exactly the same as your rate base is, so that financing of a receivable and financing of a capital asset, the source that financed that came from both debt and equity. The weighted average cost of capital is applied to the Rate Stabilization Plan because of the fact that it's recognizing that the components that make up that plan were in fact financed that way. For instance, we may use promissory notes to finance fuel when we buy it, but eventually the promissory notes becomes long-term debt because there's

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no specific borrowing for fuel, versus borrowing to pay a maintenance cost or whatever. So it's just a pool of debt. But what you have is that we've paid for fuel and we're not going to get paid for two years or three years or four years or five years, so really have that asset financed. But the asset was financed with both debt and equity. It may not necessarily be short term, it's a combination of short and long and equity. So if we accept the premise that the assets are financed with debt and equity and your debt cost is a combination of short and long, in the determination, when you apply your weighted average cost of capital to that, that's recognizing how it is financed. I don't know if that helps or just adds more confusion to it for you, but that's basically the philosophy behind it.
Q. Yeah. I guess inherently, if you were being paid for that rate stabilization, which is there right now, you would be reducing your borrowing requirements?
A. Yes. The total -
Q. Long or short term?

MR. ROBERTS:
A. Yes. The total borrowing would be less if we weren't financing the Rate Stabilization Plan.
Q. Right. So inherently it would seem to me that would reduce your debt costs and the -
A. It would reduce--if we never had the Rate Stabilization Plan, if we were paid 100 percent, if you looked at our debt to capital structure, it would be better.
Q. Right. Because your debt -
A. Because -
Q. Because your debt would be better?
A. Because this is debt that exists out there.
Q. Right.
A. And, of course, it's also impacted in the ratios.
Q. So that's why I would have thought the cost attributed to that would be the cost of debt as opposed to -
A. But recognizing that it's financed with both.
Q. With both, okay. The third--it's, I guess a result from a discussion that you had, I think it may have been Mr. Browne, it relates under your CA-143. I'm looking at page 51 of the October the 14th transcript, Mr. O'Reilly.

It's referring to CA-143. It's beginning on line 1. And it refers to the spiking in the rates in customer service spiked to 874. And I believe without referring back to that, although we can, I have it here, it shows it going up in 2001, 361, 427 in 2000, in that vicinity. And your comment was that it relates to collection, difficulties in collecting debt or collecting revenues in Sheshatsheit.
A. That's correct.
Q. And you seem to refer later on to the fact that this is really relating to closely one year's debt. It may be somewhat over a year, but I think you indicated it was--it would go back a year or so. Is that difference which would roughly be versus 2001 a half a million dollars, does that all relate to that? It seems to be a rather high amount. And I guess my question would be on a go-forward basis what's being done to collect that in the future versus what's been done in the past?
(1:00 p.m.)
A. Every effort that we possibly can to collect it is being explored. And I thought I had the

answer. The majority of that increase would be associated with a provision for potential bad debts associated with the accounts in Sheshatsheit.
Q. Majority of the half million dollars?
A. Yes.
Q. Yeah, I see. So is that--and it would relate to a year or slightly over a year's bad debt?
A. That may be over a couple of years.
Q. Okay.
A. We are having extreme difficulty in trying to collect the accounts.
Q. Is that something which is likely to be systemic on an ongoing basis?
A. I think the issue is going to be far reaching than just the payment of their electricity account.
Q. Okay. I understand. Okay. The other point, and maybe you could just give me a little bit of additional information, last time I queries Mr. Osmond back on November the 26th of 2001. I think the discussion was at that time that 30 percent of the employees in Hydro may very well be looking at retirement over the next five years. I think that's down to 25 now

we're talking about. The question I think I put to Mr. Osmond at the time was this would have some implications in terms of succession planning within the organization. And I think he felt at that point in time that it was an important issue, indeed, something that would have to be looked at. Could you update me if there's anything particularly being done? I notice just from the executive alone there's a fair change since -
GREENE. Q.C.:
Q. Succession planning has worked.
CHAIRMAN:
Q. - since the last time.
A. I guess it is under advisement at Hydro, looking at the ramifications of what's coming up in the next period of time. Because as Mr. Wells--there is 25 percent of our workforce will be eligible to retire. That doesn't mean that they all will and they won't be replaced. But I think there is some preliminary discussions going on as to what can be done in certain key areas as to how things can be looked at in the eventual likelihood that people do retire and at certain times. But

MR. ROBERTS:
there's not a formalized study if you're referring to that. I think it's the awareness and the review and the preliminary discussions that are being done in human resources as to what may or may not be the issues and what may or may not be some of the solutions to deal with it.
Q. It's going to have a very significant impact not only for Hydro, but other organizations as well. There's nothing formal being -
A. It's nothing formal. It's strictly at the discussion level at this point.
Q. Okay. That's all the questions I have. Thank you, very much, Mr. Roberts. Are there any questions arising from any of that? Mr. Browne, good morning.
BROWNE, Q.C.:
Q. Just in reference to a question that Commissioner Saunders asked re contracting out and a follow-up in reference to tracking of expenses that the Chairperson asked. In applying contracting out and tracking of expenses in reference to CF(L)CO, is that a delicate situation there where you have the

minority shareholder, Hydro Quebec, in terms of if you attempted to contract out or you attempted to get more revenue than what you're getting now in the current system, couldn't the minority shareholder say we could provide that for equal or less than what you're looking for?
A. I guess it's a difficult question for me to answer. I think Hydro Quebec could certainly say, yes, maybe we could provide that service. To date that hasn't happened. They do this review based on the information that's provided to them. And what we've seen earlier this morning on the analysis of the question, they are provided with more information than what was shown on the screen so they have an explanation as to what's into the cost as well as if there's an increase or a decrease. And we do ask them to formally approve the administrative services agreement for that particular year. But at this point they haven't, that I'm aware of, had suggested that anyone other than Newfoundland and Labrador Hydro would complete these services for CF(L)CO.

Q. Thank you.
CHAIRMAN:
Q. Thank you, Mr. Browne. Mr. Kelly?
KELLY, Q.C.:
Q. Thank you. Mr. Roberts, I have just have a couple of questions about Hydro's short-term borrowing and the promissory notes. Are those promissory notes issued to a financial institution or is the money borrowed from government by issuing the notes to government?
A. It would be borrowed from financial institutions, not government.
Q. Sorry?
A. It's not borrowed from government.
Q. So it's financial institutions, it's -
A. That's correct. It could be Royal Bank, could be Bank of Nova Scotia, could be those types of financial -
Q. That's my next question. Is it one financial institution -
A. No.
Q. - or is it a series that you go to the market at any point in time?
A. It's a series. We actually have a listing of the people that would issue promissory notes.

And what we do is we go through and we place calls and say, look, we need $100,000 for a period of time, what's the rate.
Q. Right.
A. And then it would be based on the analysis of that rate and whether or not they could provide the requirement that we're looking for, we'd make the decision as to who would receive the promissory note.
Q. And is there a minimum or usual amount that you would to go? You referenced $100,000 a few moments ago. Are they ordinarily issued in denominations of 100 or -
A. No, no. It's a function of the daily monitoring of the cash requirements that would dictate the amount of promissory notes.
Q. But is it like--is there a--obviously you wouldn't go for $500 or -
A. No, no.
Q. So is there a kind of minimum usual level? Just to help us with understanding the process.
A. The reason why I'm hesitating because I see promissory notes for more than one company. I would suggest to you that we'd be talking in

MR. ROBERTS:
the hundreds of thousands as they're being issued, not down below that, a smaller number.
Q. Okay. That's fine. Thank you, Mr. Roberts.
CHAIRMAN:
Q. Mr. Kelly. Mr. Seviour?
MR. SEVIOUR:
Q. Nothing arising.
CHAIRMAN:
Q. Thank you. Mr. Kennedy?
MR. KENNEDY:
Q. Nothing arising, Chair.
CHAIRMAN:
Q. Ms. Greene?
GREENE. Q.C.:
Q. I have a couple arising. Thank you. The first one relates to succession planning. I wanted to bring you back to comments you had made earlier in response to questions somebody asked you today on the apprentices. And you indicated at that time Hydro had increased the number of apprentices since 1997, '98. Could you advise the Board as to why Hydro had increased the number of apprentices?
A. Part of the reason it had increased the number

of apprentices is, as I was saying, related to your so-called succession planning and the replacement of your line workers and your other trades people towards the future. Hydro has increased its level of apprentices in anticipation of this is what's going to happen, recognizing that, yes, there is a two-year apprenticeship period or a three-year apprenticeship period, no guarantee at the end of that period, but we are having these people throughout the system and they may be able to avail of full-time opportunities as they arise.
Q. So that was done in contemplation of the retirements coming up in the trades, is that correct?
A. Yes, it was.
Q. So that's a form of succession planning Hydro has engaged in recent years?
A. Yes.
Q. Okay. At the trades level?
A. Yes.
Q. The next couple of questions relate to questions from the Chair. And first with respect to the business process improvement.

You mentioned there was no master list of processes that are to be reviewed. Could you indicate, though, for the Board what are the processes that are under way now in 2003 and what's planned going forward?
A. The three main processes that are under review right now, as I mentioned earlier, was the acquisition of the goods and services which also entails the organizational structure relative to the centralization of inventory control. The second process that's being reviewed which is referred to as the work management, that's dealing with the work identification and execution as well as the budgeting for those work activities. And the third process that's under review is referred to as asset management and this is financing of the capital asset records with the equipment records.
Q. Mr. Roberts, do you know the anticipated schedule for those three processes, process reviews?
A. It is anticipate that these projects, some of which will be finished in 2004 and some may extend past 2004.

Q. So the processes to be reviewed have been determined for the balance of 2003 and into 2004, is that correct?
A. Yes, it is at this point.
Q. The next comment, I guess, was from--question arises from the comment of the Chair that there doesn't appear to be much paper with respect to BPI (phonetic). And I think there maybe some confusion between Mr. Wells' comments with respect to formal report, because Mr. Wells also talked about there was a lot of diagrams and charts on the wall when the people came up. So I wanted to review with you, very briefly, how the process--for example, let's take one that you're familiar with, the accounts payable process. Can you just give an outline for the Panel members as to how the process is reviewed and what the management team would have looked at before the decision was made to proceed?
A. Well, in the case of the accounts payable process, the employees were asked to quantify where they were spending their time and then the actual main processes within the accounts payable system were identified and were

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MR. ROBERTS:
actually flow charted showing the flow of the information through the system and what happens at critical points. And from that it was identified that there was what we would refer to as re-work happening. And what I mean by re-work is a wrong code requiring information to be sent back to somebody else to be corrected. Through that process and the allocation of the time, it became evident that if you were able to eliminate having to do some of this re-work and could change the process, then there would be inherently savings in the time that would be available. With these estimates of time being developed as to how much was being spent into particular areas, you were able to say, well, if you're spending three days a week tracing down vouchers that have been sent back to the field for re-coding, and if we eliminate that process, then there's three days that have been saved of time that will either be a true saving or it can be better utilized in value-added work, rather than non-value-added work. So it was those types of high-level estimates

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that were used and presented to management, as Mr. Wells was saying, in most cases via slide show, saying look, you know, here's the flow chart. They've actually brought them into the room and put them on the wall and said, look, you can see for yourself and spend some time to see exactly what's happening. And then based on the quick analysis of what's been done, you know, we had the opportunity here to say in these particular areas, and there can be a benefit. And of course, based on that, you can see that there would be anticipated savings that would be--arise. So once the decision was made to proceed with those reviews and to implement those changes, then the team would go through and do the analysis and say, okay, well, this is the way that the process gets resigned--redesigned to achieve the savings that were anticipated.

Q. So I understood from your answer that there would have been a description of the process outlined on paper with an estimate of the savings before there was--at the first stage, is that correct?

A. Yes.

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Q. The second stage would be again on paper where the redesign process was outlined to management, is that correct?

A. Yes, as to what could be changed and what the new process would look like.

Q. And at that time was there an estimate of the anticipated benefits that would be achieved if the process was redesigned?

A. Yes, there would be an estimate of the amount of savings that could be achieved if the redesign of the process could be completed as being presented.

Q. And after--I'll stay with the one you're talking about, the accounts payable, which has been one that has been implemented. After the redesign process was implemented were, in fact, the savings achieved and what did you do to determine that?

A. What was done is that we looked back at what was anticipated and what were the changes that were required to be done and what was actually done at the end of the day. And in the case of the accounts payable it actually ended up eliminating approximately one and a half positions just from the redo of some of the

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elimination of the items and the redesign in the accounts payable section.

Q. So there was a reduction achieved as has been estimated, is that correct?

A. Yes.

Q. And that was salary savings?

A. That was primarily salary savings.

Q. So with respect to the process, the charting of the existing process and the redesign of the new process, was that done in paper that was available for your review?

A. There was other commentary that was provided during the analysis and the discussion, but the prime thing was showing here's what the current process exists like and here's how it could be changed.

Q. So that was the source of Mr. Wells' comments that there was lots of charts and diagrams and -

A. Lots of charts and diagrams -

Q. - and flow charts?

A. - that went around the room, actually, and behind the door in some particular cases.

Q. Thank you. That concludes my questions.

CHAIRMAN:

Q. Thank you, Ms. Greene. That was useful for me. Thank you, once again, Mr. Roberts, very much. We will adjourn for today and we'll reconvene with Mr. Haynes at 9:00 on Monday morning.

Upon concluding at 1:19 p.m.

CERTIFICATE

I, Judy Moss Lauzon, hereby certify that the foregoing is a true and correct transcript in the matter of Newfoundland and Labrador Hydro's 2003 General Rate Application for approval of, among other things, its rates commencing January, 2004, heard on the 16th day of October, A.D., 2003 before the Board of Commissioners of Public Utilities, Prince Charles Building, St. John's, Newfoundland and Labrador and was transcribed by me to the best of my ability by means of a sound apparatus.

Dated at St. John's, Newfoundland and Labrador this 16th day of October, A.D., 2003

Judy Moss Lauzon