

1 Q. On page 5 of the report entitled *Strategic and Business Planning Processes*
2 *for Newfoundland and Labrador Hydro* dated December 2004, Hydro's core
3 businesses include merchant plant "construction, operation and maintenance
4 or power production and related transmission facilities intended primarily to
5 exploit natural resources for export". Please provide a copy of the report and
6 please provide a detailed list of Hydro's initiatives in this core business area.

7
8
9 A. The report Strategic and Business Planning Processes for Newfoundland and
10 Labrador Hydro is attached.

11
12 On behalf of its shareholder, the Government of Newfoundland and Labrador,
13 Hydro is currently pursuing the development of the Lower Churchill Hydro
14 Project and is also exploring the feasibility of developing large-scale wind
15 generation in Labrador. If developed, a portion of the output from these
16 developments could be dedicated to the export market.

17
18 Hydro has also entered into an agreement with Hydro-Québec, which will
19 facilitate the delivery of electricity to the Shefferville area of Québec via the
20 Menihek hydroelectric generating station in Northern Labrador. Work is in
21 progress to acquire these assets from IOC, the current owner.



**Strategic and Business
Planning Processes
For Newfoundland and Labrador Hydro**

Pursuant to Order No. P.U. 14 (2004)

Newfoundland and Labrador Hydro

December 2004

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Introduction

In Order No. P.U.14 (2004), the Board of Commissioners of Public Utilities (“the Board”) directed Newfoundland and Labrador Hydro (“Hydro”) to file, by December 31st, 2004, a report outlining:

- “i. a comprehensive description of Newfoundland and Labrador Hydro’s strategic and business planning processes; “*
- ii. a description of how corporate goals and strategies are communicated and operationalized, including how specific operational targets are identified and linked to corporate goals and strategies;*
- iii. a description of how management performance and employee incentives are tied to achieving targeted goals, outcomes and efficiencies.”*

This report is filed in response to the Board’s direction.

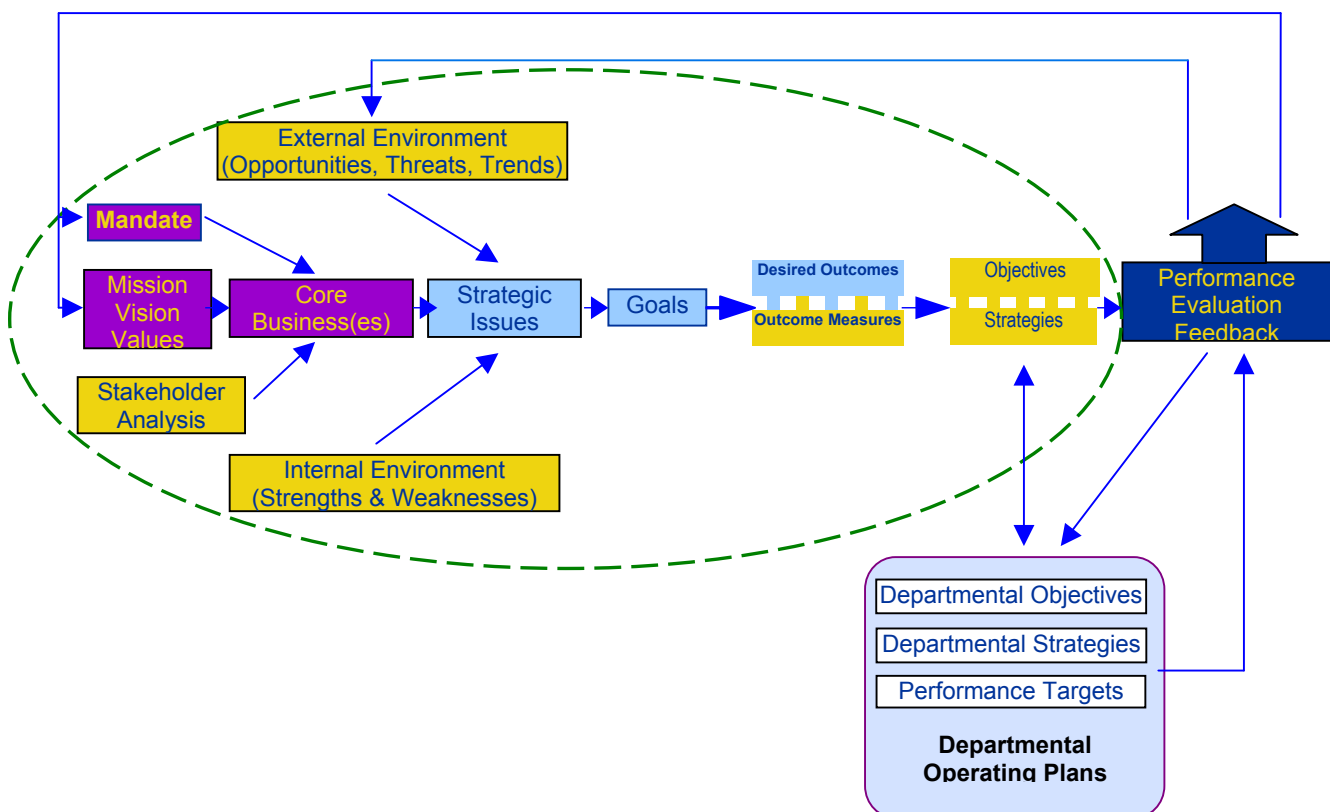
i. Strategic and Business Planning Processes

In 2000, following the installation of a new computer system, supporting an integrated suite of software applications from JDEdwards, Hydro began a thorough review of its strategic plans and its strategic planning process. The review of the strategic planning processes focused on the incorporation of strategic thinking and planning in the culture of the Hydro Group. It was intended to foster the creation and stimulation of a strategic dialogue throughout the Corporation, to ensure a focus of activities, decisions and resources on the critical issues and opportunities.

The initial discussions involved senior management, approximately twenty (20) individuals, who met regularly over a period of months to develop a strategic planning framework and the basic strategic issues. The process was detailed and comprehensive. The discussion was expanded to approximately seventy (70) management positions and eventually the developed initial plans were introduced to all employees at special sessions throughout 2002, for comment, refinement and adoption. Subsequently, within each division, smaller breakout sessions were held with employees related to the development of objectives and strategies with respect to the achievement of defined goals.

The whole process was conducted within the following framework, starting with the review of Hydro's mission and mandate, the development of a new vision and values and, following extensive analysis, the definition of the core strategic issues and goals for the Corporation.

Table 1
Strategic Planning Cycle



The exercise resulted in a comprehensive methodology to ensure that strategic planning continues to set the parameters for the activities undertaken within the Corporation and that it is the principal guide in focusing activities within the Corporation. The strategic plan allows corporate issues and goals to be addressed over an extended period of three to five years, supported by shorter term goals, objectives and work plans within an annual planning cycle.

Since 1996, corporate and divisional objectives for the ensuing year have been developed by Management and confirmed by the Board of Directors. As well, the results of the previous year's corporate and departmental objectives are reviewed with the Board of Directors. The content of this process is outlined in an annual document addressed to the Board of Directors. This practice continues, and since 2001 has become part of the overall strategic planning cycle within the organization.

The following is the summary of the outcome of each phase of Hydro's strategic planning review from the establishment of a new vision for Hydro through to the determination of the identified corporate strategic issues and goals.

Vision:

Hydro's vision is to be recognized as an innovative and quality energy services provider.

Mission:

Newfoundland and Labrador Hydro is a crown corporation committed to providing cost-effective and reliable energy services to our customers for the benefit of all people of the province.

Our skilled and committed employees will use innovative methods and technologies, and will maintain the highest standards of health and safety and environmental responsibility.

Values:

The fundamental truths and principles practiced by Hydro and its employees in providing quality service to all its customers and stakeholders:

- **Integrity** - trust, respect, honesty and fairness are essential in our daily interactions with all individuals and stakeholders.
- **Responsibility** - we value actions that are ethically, environmentally and socially responsible.
- **Teamwork** - we promote safety and health, cooperation and openness in a supportive work environment.
- **Competence** - we encourage and support innovation, continual improvement and learning, and the sharing of our knowledge and experiences.
- **Accountability** - we accept responsibility for our individual and collective actions and performance.
- **Positive Attitude** - we value enthusiasm and pride in our work.

Core Businesses:

- **Generation** - production or purchase of electrical energy from various sources that are environmentally and economically sound, reliable and intended to supply the needs of residential as well as industrial development in Newfoundland and Labrador. There are two aspects of generation – Hydro and Churchill Falls (Labrador) Corporation (“CF(L)Co”) – with the difference being that CF(L)Co is primarily export, after the Labrador interconnected loads are supplied.

- **Transmission** - delivery of electrical energy to wholesale, industrial and distribution centres across the province.
- **Distribution** - delivery of the electrical energy from the isolated generation plant or from the delivery point from the transmission system to the residential and commercial end use customer in our geographic area of operation.
- **Merchant Plant** - construction, operation and maintenance of power production and related transmission facilities intended primarily to exploit our natural resources for export.

Strategic Issues:

- **Clarification of Role of Newfoundland and Labrador Hydro**

Clarifying the future mandate and direction of Hydro and confirming this direction with the provincial government is the primary strategic issue facing the Corporation. Resolving this issue will effectively define, at a high level, the future of the Corporation and is the basis for establishing more detailed priorities and implementation plans.

- **Performance**

Improving performance has been identified as an issue that relates to all levels of Hydro – corporate, departmental, team and individual, and all activities – core business and support.

The Corporation recognizes that focusing on processes, resource planning and technology are critical areas to be addressed in order to improve performance. With respect to processes, a structured approach to process review and improvement is seen as a tool to improve performance by allocating resources in a manner that reflects corporate priorities and thereby operationalizes the

strategic plan. Information technology integration and utilization to support decision-making is also critical to achieving improved performance.

- **Corporate Culture**

Hydro recognizes the need to evolve to a corporate culture that focuses on customers, supports strategic thinking and promotes a more proactive approach to identifying and addressing issues and opportunities. As well, the corporate culture of the future will be more performance-focused and will place increased importance on communication and morale.

- **Regulatory Framework**

Hydro recognizes the opportunity to influence the evolution of the regulatory framework and to thereby assist in creating a climate that promotes innovation and efficiency. In this regard the trends in other jurisdictions, including streamlined reporting requirements and performance-based rate setting, may be of particular interest.

- **Public Image**

Hydro recognizes that there is limited awareness or understanding of its role and the benefits it provides among external stakeholders. Enhancing the public image of Hydro will affect the ratepayer and shareholder view of the Corporation and will also impact employees' perspective. As with other strategic issues, the relevance of public image increases in the current operating environment.

- **Growth Strategies**

Identifying and pursuing opportunities for renewed growth may be part of the future role of Hydro. The opportunities for growth for Hydro could relate to

industry structure rationalization, pursuit of export markets and/or expansion to other services (eg. telecom, engineering). The Corporation's role in specific developments, including Muskrat Falls and Gull Island, is also part of the issue of growth. These developments in particular and the general matter of renewed growth are seen as significant matters to be addressed in defining and confirming the future role of the Corporation and thereby impacting the business operations, culture and climate of Hydro.

- **Customer Service**

Hydro's customers include its external customers as well as internal customers. External customers include direct customers - interconnected rural customers, Newfoundland Power and industrial customers as well as indirect customers – ratepayers who are served by Newfoundland Power. The Corporation recognizes that a proactive approach and focus on customers and customer service is an integral part of a commercial enterprise. In addition, the Corporation recognizes that there is a need to recognize the importance of satisfying internal customers as part of a customer service focus or orientation. While the importance of serving customers is an underlying theme reflected in other issues, it has also been acknowledged as a key challenge that must be elevated and addressed in order for the Corporation to achieve its future state.

- **Human Resource Requirements**

The employee group at Hydro is aging and in the period from 2004-09, approximately 25% of staff complement will be eligible for retirement. The availability of the appropriate number of employees with the required competencies to fulfill Hydro's future role is a strategic issue to be addressed over the planning period. A human resource strategy that addresses succession requirements in the context of Hydro's future role has been identified as a response to this issue.

Following the determination of the corporate strategic issues, the following were the initial goals agreed upon to best achieve the strategic issues.

Goals:

1. To operate in a commercially oriented manner within the clear policy direction and regulatory framework established with the owner.
2. To be a customer-focused corporation.
3. To optimize corporate performance.
4. To have a dynamic and innovative work environment where employees are challenged and recognized for their contribution.
5. To increase public awareness and to be trusted and respected by our stakeholders.
6. To increase income opportunities from the diversification and expansion of energy and related services.

In Order No. P.U. 14, the Board stated it: *“had not seen a comprehensive plan from NLH that clearly integrates the overall corporate goals and strategies and the various process improvement initiatives referenced during the hearing.”* To ensure that the Board has a clear understanding of how the strategic planning process is working within Hydro, the following is an outline of the activities developed in relation to Corporate Performance and the measurement of that performance, which is a critical area of the Board’s review.

As noted above, one of the major corporate issues developed during the strategic planning review was performance. Hydro recognized that focusing on processes, resource planning and technology are critical areas to be addressed in order to improve performance. A structured approach to process review and improvement is seen as a tool to improve performance by allocating resources in a manner that reflects corporate

priorities and thereby operationalizes the strategic plan. Information technology integration and utilization to support decision-making is critical to achieving improved performance.

The goal set out in relation to this issue, identified as Goal No. 3 is:

“Optimize corporate performance”

Under Goal No. 3 the following Desired Outcomes were established.

1. Healthy Financial Performance
2. Optimal Asset Performance
3. Optimal Customer Service
4. Optimal Environmental Performance
5. Optimal Safety Performance

For Outcome 2, Optimal Asset Performance, the following objectives were set:

- to achieve agreement on measures and indicators and to finalize decisions on COPE measures.
- to assess business processes across all departments to determine process changes necessary to optimize corporate performance as determined by key indicators.

Strategies:

The strategies developed to support the objectives for Optimal Asset Performance were:

- key performance measures established for internal assessment and agreed with the Board for regulatory assessment.

- perfecting performance measures throughout the Corporation as required, including an assessment of appropriate benchmarking databases on a corporate-wide level.
- review and refine business process improvement methods, including assessment of progress made to date, format for going forward and bring process improvements to departmental levels, including accountability and performance measures.
- ensuring all efforts are aligned with strategic issues, and corporate objectives and strategies.

In reference to the third paragraph above, the strategies to review and refine business processes were developed principally through the program defined as the Business Process Improvement initiative, one of the principal programs to ensure the attainment of Goal No. 3 and ensure that the corporate issues of improved corporate performance is realized.

The **Business Process Improvement (“BPI”) objective** was defined as:

“to redesign business processes and implement changes which will drive improvement in corporate performance.”

The optimization of corporate performance was introduced as one of the 2002 annual corporate objectives and has remained as an annual corporate objective since then, as the business process improvement is of necessity a multi-year program.

The following is a summary outline of business process improvement as it has developed over the past two years and proceeds to implementation in 2005 for the segments identified. When fully implemented, it will alter the approach to how work is identified, prioritized, budgeted, executed and measured within the Corporation. As well, it will

provide the basis for internal measurements and assessments and external comparisons, which is a significant corporate strategy issue of relevance to the Board.

Beginning in 2002, the BPI initiative addressed eleven (11) processes and one enabler. Seven of the twelve have been redesigned. They are: Goods and Services, Materials, Consumables, Purchasing Card - Travel, Accounts Payable, Asset Record Management and Work Execution. The following processes are now in development prior to implementation. They are: Contract Management, Work Identification and Prioritization, Work Budgets, and Outage Management.

The following is a brief outline of the purpose and intent of each process. Comment on the Work Budgets Process, as an example, describes more completely what the content of a specific process review encompasses.

Goods and Services Process:

The purpose of this process review was to ensure that materials and services are available to the workforce as planned within the published lead times, and allow for emergency and urgent work.

Materials Process:

The purpose of the materials process was to ensure that material classifications are managed effectively and efficiently to meet the requirements of the core business at least cost.

Consumables Process:

The purpose of this process was to manage low cost, high turnover items to minimize administration and increase productivity.

Purchasing Card And Travel Processes:

The purpose of this process was to minimize the administrative cost to both travel expense disbursements and low cost material purchases.

Contract Management Process:

The purpose of this process is to develop a consistent and effective means to manage contracts from project initiation to completion.

Accounts Payable Process:

The purpose of this process review was to ensure disbursements are made within acceptable accounting practices at least cost.

Asset Record Management Process:

The purpose of this process was to provide accurate integrated asset records containing financial and maintenance information, links to inventory, cost of service requirements and ease of information retrieval.

Work Identification and Prioritization Process:

The purpose of this process is to ensure that only work of the highest value, consistent with the corporate strategic direction, is submitted for approval.

Work Budgets Process:

The purpose of this process is to create a work master plan schedule, master resource plan and master procurement plan prior to final preparation of operating and capital budgets. This will result in a master work plan and schedule identifying work to be done in the immediate year and in each of the next five years. The master resource plan will identify all labour (internal and external), special tools, equipment, and vehicles (including cost estimates). The master procurement information plan will identify goods and services

having long lead times, common to multiple areas, on a recurring basis, and items resulting in extraordinary demand on inventory.

Capital and Operating budgets will be in a standardized format reflecting the approved work plans. This will enable cross-divisional reviews and prioritization permitting timely communication with information visible at all levels. A work plan and budgeting tool set enabler will be linked to the JDEdwards system.

Implementation of the improvements in the process will result in a reduction in the hours of rework involved in the budgeting process. In addition, procurement information supplied to materials management at least nine months in advance of the time it is required, will allow for the opportunity to improve procurement practices to ensure on-time delivery at the lowest cost. The master work schedule and a labour resource plan will align work requirements; any constraints that may be required or affect the work; and, the labour resources required to perform the work. These plans will provide an opportunity to maximize the utilization of resources by significantly reducing conflicts between work requirements, constraints and resources. Planners will have adequate time to ensure all is ready to execute the plan, thus avoiding any delays and associated costs. The target implementation date is December of 2005.

Work Execution Process:

The purpose of this process was to ensure that the Corporation achieves maximum utilization of human and physical resources, resulting in increased productive wrench time.

Outage Management Process:

The purpose of this process is to ensure that asset outages are effectively managed from work identification and prioritization to work execution by optimizing asset performance and resource productivity.

Enabler Technology:

In support of these work processes, particularly Work Budgets and Work Execution, enablers have been developed to permit software applications such as the JDEdwards Integrated Suite to perform tasks in support of core and support processes. The purpose of the JDE enabler is to achieve both the financial and work management requirements of the organization to enhance decision-making capabilities.

Process Review Summary:

Each process review has resulted in an extensive and detailed analysis of the work, how it is performed, and the measures to be taken to improve performance or provide a basis on which improvement can take place. Each area of process review is interrelated with the other and it will take time for the results to become fully realized. For example, the identification of work and the prioritization of that work will lead to improved budgeting, and planning for the execution of the work. The standardization of procedures throughout Hydro will ensure that common standards will permit process metrics to be established and eventually standards redefined. The development of reliable standards related to the actual work to be performed within Hydro will have a significant effect on future performance including an objective measurement of that performance. It will also provide the basis and framework to move Hydro in the direction of “asset management”, including the refinement of maintenance philosophies for various asset types. Fundamental to the whole of the program is the recording of all costs related to any asset, whether capital or operating, during the life cycle of that asset.

Supervisors, managers, planners and front line supervision will have access to all the pertinent data as required to enable them to track and record all costs associated with the work activities under their control and as well, they will be able to properly monitor work in progress.

Corporately, planning and budgeting will have a much greater degree of certainty over an extended horizon which will provide more certainty with respect to forecast costs of operation and revenue requirements. The result includes more useful data for detailed financial planning related to asset maintenance and operational costs.

Performance Indicators

In tandem with the BPI initiative, a committee was established to identify the Key Performance Indicators (KPI), which has led to the KPIs adopted by the Board and Hydro during the last rate hearing as expanded in conjunction with the Board's advisor, Grant Thornton. This process has continued with the development of the additional KPIs directed by the Board in P.U. 14.

Hydro's program to optimize corporate performance will result in ensuring that Hydro operations in providing electricity and services to its customers, are in accordance with its legislative mandate to operate in the *"most efficient production, transmission and distribution of power at the least possible cost."*

ii. Communication and Operationalizing Corporate Goals and Strategies

As stated in the first section of this Report, the corporate strategic issues and goals were communicated throughout the organization in extensive top level management meetings, three-day sessions for senior and middle management and two to three hour sessions including all employees at the company's operational centres. Subsequently, within each division, workshops were held to review strategies and objectives related to the strategic objectives and targets.

Each year, Management Committee, which includes the President and Vice-Presidents, review the corporate strategic issues, and prepare the corporate and divisional objectives and strategies for review by the Board of Directors, for both the next year and a review of

the past year. In each year, the divisional Vice-Presidents are responsible for the setting of divisional and departmental objectives, which support the corporate strategic objectives and goals. The Vice-Presidents, as a small group, are acutely aware of the corporate strategic issues. In discussions with their directors and managers, activities within a division or department are related to the strategic objectives, both long term and shorter term objectives, such as the completion of the Granite Canal Power Plant, or the upgrading of a transmission line - for example TL214. Both projects support the availability of supply (capacity) and the reliability of that supply (quality of service provided).

As provided for in the strategic planning template, annual corporate and divisional objectives, which are shorter-term objectives and strategies, are developed in support of the longer-term goals and corporate issues. The annual plans relate to the functional requirements of the operation and are focused on safety, the environment, improving the reliability of service, enhancing performance and cost reduction.

The Management Committee and directors and senior managers meet together to review ongoing strategic issues, as well as the specific programs within a division or department.

The BPI initiative is headed by a Senior Management Improvement Team ("SMIT"), which oversees the progress of each of the Process Improvement Teams. It meets weekly with the President and Vice-Presidents.

The Senior Management Improvement Team, consisting of eight (8) senior managers, provides the oversight and direction to the process improvement teams. A full-time Executive Director appointed from Senior Management manages the BPI Initiative and coordinates the work of the process improvement teams. Eleven (11) process improvement teams have engaged fifty-five (55) key employees from all areas of the organization in the process improvement initiative. To date, forty-seven (47) employees have been trained as change agents as part of the implementation of new processes, to implement seven (7) of the redesigned processes and one enabler.

In 2003 and 2004, six (6) organization-wide workshops were held having an average attendance of sixty-five (65) employees per session. These sessions were held to outline the issues, and communicate the proposed process redesigns and obtain the input from those attending to refine the process as being discussed. In addition, rollout sessions in 2002 touched approximately 80% of union and non-union employees.

In 2002 and 2003, nine (9) BPI newsletters were issues to all employees. Hydro's internal news magazine, "*THE OUTLET*", has featured articles on BPI since 2002. A new weekly one-sheet publication entitled "*THE NEWSWIRE*", which was introduced in 2004 has contained two articles on BPI. Since 2002 and the initial introduction of the strategic planning overview and the introduction of BPI, the President's annual message to all employees has referred to the strategic issues, goals and the specific objectives of BPI. As a prelude to the introduction and implementation of new processes in 2005, including work execution, work identification and prioritization and work budgets, the President with a Vice-President has conducted eleven (11) two to three hour sessions with a cross-section of employees throughout all areas of operations within the Province.

iii. Performance and Incentive Plan

A performance based incentive plan was introduced in 2001 for members of the Executive and Senior Management, including the Managers/Directors of departments, generating plants and regional areas. Both corporate performance objectives and departmental performance objectives were included in each individual's incentive plan for 2001, 2002 and 2004 while for 2003 objectives related to corporate performance only were used.

The areas selected for corporate performance each year for inclusion in the incentive plan are developed in consultation with the Board of Directors, Executive Management and the senior managers and directors. The areas selected are based upon the overall corporate objectives that are established for each year through the strategic planning

process. Specific outcomes are identified for each area with various levels of achievement being identified for different incentive payments.

Financial performance and system reliability have been two areas of responsibility that have been identified each year to date for inclusion in the incentive plan with specific targets established for each year. For example, the financial performance target is established each year based on the forecast budget and expected financial performance. With respect to system reliability, the targets selected identify an improvement in system reliability over past performance.

A third area of corporate performance which has been identified each year in the incentive plan is safety. For 2001 and 2002, the corporate targets identified related to the implementation of a revised safety plan. During this period, Hydro undertook a comprehensive review of its existing safety plan and identified a number of revisions for implementation by each department, plant and area. For 2003 and 2004, the all-injury frequency rate was selected for inclusion as a corporate area of responsibility with the targets being established as identified improvement in Hydro's past performance.

For 2001 and 2002, a fourth corporate area was identified for inclusion in the corporate areas of responsibility and that was strategic planning. During this period of time, Hydro was engaged in the introduction of a strategic planning process. Sessions were held with all employees with respect to Hydro's mission, mandate, vision, values and the identification of long and short-term corporate objectives. This process also included discussions with Hydro's Board of Directors. The inclusion of identified outcomes on this corporate area of responsibility related to the implementation of the process within each area of the Corporation.

In 2003, when corporate objectives only were identified in the incentive plan two additional areas were included: environment and customer service. With respect to environment specific outcomes were identified related to the number of exceptions that were identified in environmental audits completed under the ISO process. Hydro has

achieved certification for the ISO 14001 standard. With respect to customer service, the specific target identified was based on the customer satisfaction index as identified in the annual customer survey.

Departmental or divisional objectives were also established for 2001, 2002 and 2004 for each employee participating in the incentive program. These objectives and the appropriate targets for each were selected following discussion with the executive responsible for the area and the director/manager and related to how that department or area played a role in achieving identified corporate objectives for the year. Specific targeted outcomes were identified for each activity included within the department/divisional components of the incentive plan. Payments were based upon various levels of performance achieved with respect to the established targets. For example, if a department was involved in a significant way with respect to capital projects, targets were established with respect to the completion of projects within identified schedules and budgets. If a department was significantly involved with customer service, targets were established with respect to appropriate communication goals for the customers impacted.

At the end of each year, a review is undertaken with respect to the performance achieved with respect to each goal and target that had been identified. The results of this review are then considered by Hydro's Board of Directors.

The components of the incentive plan each year are coordinated by the Human Resources Department of Hydro and approved by Hydro's Board of Directors. Hay Management Consultants were retained originally to assist in the development of the plan for 2001 and again in 2004 to review its application in that time period. Payouts are set at 6% of salary for achievement of targeted performance, 3% for a threshold level of performance and 9% for achievement above the target. Approximately 20 executive, senior managers and directors participate in the incentive plan.