EVIDENCE
Whitehorse, Yukon
Wednesday, February 9, 2005 — 10:00 a.m.

Mr. Hardy: I will now call to order this hearing of the Standing Committee on Public Accounts of the Yukon Legislative Assembly.

Today, the Committee will investigate the Auditor General of Canada's report on the Mayo-Dawson City transmission system project.

I would like to thank the following witnesses for appearing: Mr. Willard Phelps, Chair of the Board of Directors of the Yukon Development Corporation; David Morrison, President and Chief Executive Officer of the Yukon Development Corporation; and Eric Hoenisch, Chief Financial Officer of the Yukon Development Corporation.

Also appearing as witnesses are officials from the office of the Auditor General of Canada. They are Ronald Thompson, Assistant Auditor General responsible for Territorial Governments; Eric Hellsten, Principal in the Vancouver office; and Gerry Chu, who is a director in the Vancouver office.

I will now introduce the members of the Committee and its advisors. The Committee members are me, Todd Hardy, the Chair of the Committee; Patrick Rouble, who is the Vice-Chair; and Brad Cathers and Steve Cardiff.

Advising the Committee today is Roger Simpson, who is a principal in the Edmonton office of the Auditor General of Canada, and Monica Reda, who is an audit project leader from the Vancouver office.

The Clerk to the Public Accounts Committee is Floyd McCormick.

The Public Accounts Committee is established by order of the Legislative Assembly. We are a non-partisan committee with a mandate to ensure economy, efficiency and effectiveness in public spending — in other words, accountability for the use of public funds.

Our task is not to challenge government policy, but to examine its implementation. The results of our deliberations will be reported back to the Legislative Assembly.

To begin the proceedings, Mr. Thompson will give an opening statement summarizing the findings in the Auditor General's report.

Mr. Morrison will then be invited to make a brief opening statement. Members will then ask questions.

Our plan is to conduct this hearing from 10:00 a.m. until noon, and then from 1:30 to 3:30 this afternoon. Nonetheless, I ask that questions and answers be kept brief and to the point so that we may deal with as many issues as possible in the time allotted for this hearing.

At the end of the hearing, the Committee will prepare a report of its proceedings and any recommendations that it makes. This report will be tabled in the Legislative Assembly along with a verbatim text of the hearings.

We will now proceed with Mr. Thompson's opening statement.

Mr. Thompson: Thank you very much, Mr. Chairman, and thank you for inviting us here today to discuss the Mayo-Dawson City transmission system project, which was completed by Yukon Energy Corporation — I'll refer to it as YEC, a subsidiary of the Yukon Development Corporation.

We undertook the audit of the Mayo-Dawson City transmission system project at the request of the YEC Board of Directors. The project was essentially justified on the basis of cost-savings that would result from replacing diesel-generated power with hydro power to provide electricity to Dawson City customers. The work was originally planned to be completed before the end of 2002.

Overall, we found that the corporation did a poor job of planning and implementing the project. There were significant delays and significant cost overruns.

Mr. Chairman, I would like to go over our findings briefly just now. From the beginning of the project it was poorly managed by YEC. We found that the project's scope and costs were not adequately defined and budgeted for in the feasibility and cost analysis. For example, cost estimates did not clearly identify potential project costs such as legal and insurance costs during construction.

We found that the corporation did not have the required experience and expertise to carry a project of this nature and this magnitude. We also found that Yukon Energy Corporation's board of directors was not fully briefed by management about the risks of using the chosen construction method, something called design/build.

The corporation did not apply good project management practices. It did not have a project management policy and so it lacked clear standards and procedures to implement this project. For example, there was no project brief with a statement of objectives that clearly defined roles, responsibilities, accountability, implementation approach, detailed budgets and controls for this project.

Numerous problems were encountered during project implementation. For example, there was trespassing on First Nation lands and the transmission line had to be rerouted around the Dawson City Airport. These problems resulted in additional costs, unresolved disputes between the corporation and the construction contractor and completing the project one year behind schedule.

We identified significant deficiencies in contracting for construction and services. There was no established contracting policy and no clear contracting procedures for Yukon Energy Corporation staff to follow. We found that the corporation did not appropriately consider retendering the construction contract, despite concerns about the contractor's proposal and experience.

For this project, the corporation awarded 12 contracts, each with payments over $50,000, without competition and with no explanation in the corporation's files to justify this approach. We also found that the contracts with the project manager and the project engineer did not include adequate safeguards to protect the interests of the corporation.

In addition, the contract for project engineering services was not properly planned and was not properly authorized. Finally, financial management and project cost controls, in our view, were also inadequate. For example, internal costs incurred on this project, including project management and corporation staff costs, were not properly controlled. Formal change orders were not made for work performed, and cost overruns were not properly approved or authorized.

The corporation indicated that the total cost of the project would be about $36.2 million, representing a cost overrun of about $7 million. Our audit concluded that the final cost may even be higher.

Essentially, the corporation did not follow basic project management principles. In the end, it does not appear that the corporation received what it had contracted for. The construction agreement specifically stated that the corporation's intent was to receive first-class design and construction work. We don't believe that this was received.

Mr. Chairman, that concludes my opening statement, and we will be very pleased to answer questions or participate in any other way during this hearing.

Thank you very much.

Mr. Hardy: Thank you, Mr. Thompson.

Mr. Morrison.

Mr. Morrison: First of all, we would like to thank the Committee for the opportunity to be here today to discuss the Auditor General's report. It was back in November of 2003 that the board of the corporation wrote to the Auditor General and asked her to conduct a special examination audit of this project. It was the board's very strong feeling at the time that an independent and very objective look at the project was required in order to sort out, on a go-forward basis, how this project got itself into problems and what those problems really were.

I know that we will have an opportunity today to answer questions from members of the Committee. I would like to say that we are very pleased with the work that the Auditor General's office did. I think that in the end it will prove to be of great assistance to the corporation. We are happy to answer any questions from the Committee.

Mr. Hardy: The questioning will begin with Mr. Cardiff.

Mr. Cardiff: I'd like to thank the witnesses for appearing here today, and I hope that we can sort some of this out today and provide an explanation to the public about what actually happened here.

We'd like to start this morning, for the benefit of the listening public and citizens of the Yukon, to ask Mr. Morrison or Mr. Phelps to provide us with an overview of the history of the Yukon Energy Corporation, including when it was created, the purpose for which it was created and how it has evolved to its present form.

Mr. Morrison: I'll start, and I'm sure if there is something Mr. Phelps can add, he can jump in.

The Yukon Energy Corporation was created as a result of negotiations between the territorial government and the federal government which went on approximately in 1987 regarding the sale of the assets of the Northern Canada Power Commission.

The Northern Canada Power Commission was a federal Crown corporation, which provided electric utility services across the north. In 1987, a decision was made by the federal government to divest itself of this Crown corporation. Negotiations first began with the Yukon government to sell the assets that were located in the Yukon, and then subsequent to that, there were negotiations with the Northwest Territories government to sell those assets.

So the Yukon Energy Corporation was set up in order to receive those assets and to manage them. In the early years of the corporation, and from the beginning of the sale agreement between Canada and the Yukon government, the assets were rolled into the Energy Corporation but were managed by contract with Atco Yukon Electrical. For the period of time from 1987 onward, until 1998, Atco Yukon Electrical managed the assets and ran the system belonging to Yukon Electrical on a contract. In 1998, the parties being Yukon Development, Yukon Energy and the Yukon government and Atco, decided not to renew the contract and Yukon Energy Corporation was set up as a stand-alone business entity, fully staffed and managing its own assets.

That's the situation today. The corporation is operated by a board of directors, which is responsible to the board of the Development Corporation. It is fully staffed and has operated since 1998.

Mr. Cardiff: I have just a quick follow-up here on this. During the 10-year period that it was managed by Atco Yukon Electrical, it was still overseen by a board?

Mr. Morrison: There has always been an organization and a board of Yukon Energy. It would have been providing the oversight on the contract and the oversight on the financial and costs of operating the corporation, so there were some staff resources that were allocated to do that on an internal basis that would meet with the contractor and ensure that the operation was being managed to the standards that the board felt it needed to be.

Mr. Cardiff: Thank you. Could you give us an overview — again, some background — of the Mayo-Dawson transmission line project from the inception of the idea — apparently that goes back quite some time — to when it actually commenced?

Mr. Morrison: With the closure of the Keno Hill mine in about 1989, the Mayo hydro system had a surplus of about three megawatts of hydro power. Three megawatts is a little over half of the capacity of the Mayo system. In about 1991, during the period of time Yukon Electrical was managing the Energy Corporation assets, the group — the Energy Corporation/Yukon Electrical Company — took a look at the feasibility of running a transmission line from Mayo to Dawson to sell the surplus power. Through that period and into 1992, the corporations put their capital plans forward to the Yukon Utilities Board, and in examination of those capital plans it was recommended that no further work be done on the proposed transmission line until there was more demand in Dawson or until fuel prices increased. So the project has been around since 1991. It has been looked at two or three times during that period.

After 1991 and up until about 1997, electricity sales in Dawson — and I can't give you the background of why this happened — increased by some 29 or 30 percent. So there seemed to be a higher demand, so that would mean there were more sales available in Dawson, which would mean that the line would be starting to look more economic. Fuel prices also increased over that time. Then in 1998, the board of directors of YEC approved the expenditure of funds to look at a full feasibility study of the proposed transmission line, which led in 2000 to the board approving a contract for the construction of the line.

Mr. Cardiff: I think you covered everything there. I'm just wondering what the reasons were for this not proceeding prior to that. You gave some reasons.

Mr. Morrison: Just to be clear on that, Mr. Cardiff, what would have happened in 1991 or 1992 when it was being looked at as part of a capital plan is that the sales that would have been available in Dawson and the cost of fuel together would have shown that the project wasn't economic at that point. So it wouldn't go forward.

The change in that is that, as sales in Dawson went up — or potential sales in Dawson increased — and the price of fuel increased, both together again make the project economical.

Just to be clear, I don't want to be too confusing about this, but Yukon is a one-rate zone, so all the costs of operating the system are all aggregated together. In the utility field, the way we look at things is, what's our best least cost alternative? Does it cost more to generate power by a diesel generator or does it cost more to generate power by hydro, or whatever the options are? We always look at what our least cost alternative is.

Mr. Cardiff: Just one more quick point of clarification. You mentioned that the project went before the Utilities Board.

Mr. Morrison: Yes, in 1991, it was part of the capital plan that went to the Utilities Board for review, and it was both companies. Their capital plan was looked at by the Utilities Board and the decision was to not do anything further.

Mr. Cardiff: Those companies being?

Mr. Morrison: Both Yukon Electrical and Yukon Energy.

Mr. Cardiff: Can you tell us who was involved in the chain of decision making for this project? It would appear that there was a high degree of turnover in supervising the project. Can you tell us whether or not that rate of turnover caused problems for the project?

Mr. Morrison: If we go back to the point where the board of directors approved the project — so, the decision point is the summer of 2000, and management put a recommendation forward to the board for the project to go ahead and the board accepted it. At that point in time, the Yukon Development Corporation and the Yukon Energy Corporation were, for all intents and purposes, mirror companies. This is an important point, and it might be a little confusing, so please bear with me.

At that point in time, the senior management of the Yukon Development Corporation and the Yukon Energy Corporation and the board of directors were all the same people. The president of the Yukon Development Corporation was the president of the Yukon Energy Corporation; the vice-president of the Yukon Development Corporation was the vice-president of the Yukon Energy Corporation.

At that very point in time that the board was approving the project, the board also decided to split the senior management of the corporations. They decided that they needed a utility person — someone with utility experience — to run the Yukon Energy Corporation. The president of Yukon Development Corporation was still the president of Yukon Development Corporation, and that was a gentleman by the name of Rob McWilliam. They took the Yukon Energy Corporation duties away from him, and they hired a gentleman by the name of Ray Robinson to be the president of Yukon Energy Corporation. What they had done was essentially create two very different corporations now, which had almost been one corporation because the Yukon Development Corporation in 2000 essentially concentrated on Yukon Energy Corporation work. It didn't really do much else. It was involved in some other programs, but they were a pretty minor part of the work.

With the advent of this gentleman in late 2000, in the fall of 2000, around October — Mr. Robinson came from the utility business, he was an engineer; as a matter of fact. I think his expertise was in transmission projects. It seemed to me that a decision had already been made at that point to go ahead with a design/build project, but Mr. Robinson was a person who had experience in design/build projects. Unfortunately, now we've removed the president, who had been there for several years. We have a new president, and he lasted five months and was gone.

I don't know the background of why he left, but he got a job in Nova Scotia and, as I understand it, he's still there. He left here. That resulted in the corporation appointing the then-CFO, a fellow by the name of Mr. Don Willems, to the acting job of president. Mr. Willems acted in that job for quite a few months, and then he was appointed permanently in January of 2002.

So in the period of basically a year, or a little over a year, you have had three presidents, if you look at from when Mr. McWilliam left, to bringing in this Mr. Robinson, and then Don Willems. That, I believe, threw the project into a great deal of turmoil.

At the very beginning, which would have been with Mr. Robinson coming in and the project actually starting to go through the tendering and contracting phases, you've already shifted gears from one president to another, and the project was always looked at as something separate, because it was going to be design/build. It wasn't going to be the normal project; it was going to be separately dealt with, handled outside of the normal course of events. None of the staff were going to be involved because the contractor was both going to design it and build it, and so you didn't need anybody other than a project manager.

I think this whole concept of design/build, and then this change of presidents, really threw things into a confused state at the beginning. It was very difficult to understand who was in charge of the project. In addition, internally, when I say there were no staff resources allocated — there was supposed to be very little staff resources. As Mr. Thompson pointed out, the budget for internal cost was just over $1 million. Depending on who the president was — Mr. Robinson or Mr. Willems —

there were different people involved, because they had their own kind of concept of how this should have been done. So it really did create a great deal of confusion from the beginning. I think it is indicative of the project being plagued by a series of mistakes — bad decisions — and I think this was one of them.

Mr. Cardiff: That sheds a lot of light on what happened and probably raises some more questions.

In the Auditor General's report it was noted that the management and staff lacked experience to carry out such a project, and you briefly have alluded to the fact that there was somebody there who did have experience. What we would like to know today — internally, other than the president — what kind of experience did YEC have when this project was planned, and what action did it take to compensate for the lack of expertise?

Mr. Morrison: When the project was planned, as I said, by the time the decision was made to go ahead by the board in 2000, there was nobody on staff who had ever been involved in a design/build project. With the exception of the five or six months that Mr. Robinson was there, the only experience that some of the staff still with us have is working on the Mayo-Dawson line project, in terms of design/build. I think the operational staff at YEC these days were inserted into this process over the period of time to help mitigate the difficulties that were happening, but I think you have to go back to the issue of the design/build project in the beginning where there was very fundamental misunderstanding of what a design/build project is. It was clear from the outset that the contractor and YEC had very different interpretations of what a design/build project was. It set a tone, I think, from the beginning of the project, which really exacerbated the relationship over time. I mean it became difficult, to say the least.

Mr. Cardiff: Could you describe the key steps that were taken, or are taken, in the decision-making process that led to this project being approved and proceeded with? Specifically, we would like to know the process by which the minister responsible for the Yukon Development Corporation and the Yukon Energy Corporation was kept informed of progress on the project and how that minister was informed about the project and by whom — so the method and who was doing the informing.

Mr. Morrison: I'm not sure I can be as helpful as you might wish on this one, but I'll do my best. On a detailed basis, I don't know how often the management staff at YEC met with the minister. I can't tell you that. What I can tell you is the senior management — the president — in the early summer of 2000, wrote to the minister about the Mayo-Dawson project and management's plans to go forward with it and requested that the minister give approval of that decision.

Again, from the correspondence that's there, management indicated to the minister this project did not require Yukon Utilities Board approval or review, and that was their position. Their position was an interpretation of the *Public Utilities Act*, indicating it did not need — I'm trying to get my terminology right — I believe it's an energy project certificate. That's pretty much all I can tell you. I can't tell you if there were meetings or discussions — I don't know that — but they did write and advise the minister. Subsequent to that the minister gave the approval to go ahead with the project.

Mr. Hardy: I just want a clarification on what you said. You said the president and the management wrote —

Mr. Morrison: The board chair also wrote a letter, and you're right, for clarity purposes. There was a letter written by the president initially, and then the board chair. The letter from the Premier was to the board chair.

Mr. Cardiff: So, we basically have a record of how the project got started and what the minister's involvement and lines of communication were at that point. But from that point forward, is there no documentation or paper trail about what actions the board chair or the management took with respect to informing the minister about the status of the project, and how it was proceeding, or the other way as well?

Mr. Morrison: I'm not — at least today, and I'm happy to go and have a look. But I can't tell you whether or how many times the chair may have gone and met with the minister. I don't have a record of that anywhere. I can look at board proceedings and tell you whether or not there was a formal — you know, if a letter was written, but I can't recall that there was. I can't recall — and any reference to the chair briefing the minister. But that doesn't mean it didn't happen. I don't know that.

Mr. Cardiff: So there's no record of how often the board chair at that point in time would have met with the minister?

Mr. Morrison: Not to my recollection, anyway, and I'm happy to try to refresh it and, if there is, get you some additional information, but I can't recall anything.

Mr. Cardiff: We have one other question in this regard. In the Auditor General's report it talks about the fact that the design/build option wasn't necessarily the preferred choice to carry out this project. What we'd like to know is, when this project was communicated, either from management or the board chair to the minister, was the minister presented with all the options for the project, including the potential risks and benefits of each one? Or was the minister only presented with the corporation's recommended approach?

Mr. Morrison: It's my understanding that the minister was presented with the corporation's recommended approach. I want to clarify that I believe that to be the case because that's what the board was presented with. The board or the corporation was presented with management's recommended approach, as well. I think there was a very limited review at the board level of the pros and cons, but I think it's pointed out in the Auditor General's report that the board was not presented with the information that the consultants retained to do the preliminary design work and to provide some cost estimates had recommended not to use the design/build process. That was not communicated to the board.

Mr. Cardiff: So the reason the board didn't communicate it to the minister was because it wasn't —

Mr. Morrison: It wouldn't have been communicated to them.

Mr. Cardiff: To refresh our memory, when was it communicated to the minister? It was in the summer of 2000, I believe.

Mr. Morrison: It was the summer of 2000, I think in July. There was an exchange of correspondence in July and August.

Mr. Cardiff: Let me shift gears here a little bit. Can you explain to the Committee exactly what your mandate was regarding this project when you were appointed chair of Yukon Development Corporation? Why were you brought —

Mr. Morrison: When I was hired, the contractor had been removed from the project, or he was suspended from the project, and in, I think, either late 2002 or very early 2003, there was a whole series of issues. The contract was two-thirds or three-quarters done and no power was running through the line. There was a series of issues around — I think Mr. Thompson pointed out the trespass and right-of-way issues. There were local Yukon subcontractors who hadn't been paid in a couple of years. So when the government asked me to take this assignment, they indicated very clearly to me, and it's in the letter I got from the minister, that they wanted me to resolve all of the issues surrounding the construction of the Mayo-Dawson line.

That meant that when I came at the end of May 2003 — in discussions with the board and senior management at that time — I began to get involved in the project and resolving the issues.

Mr. Cardiff: I'd like to know when you actually became aware of the problems surrounding the project. Were you aware of the problems before you became chair of Yukon Development Corporation? Were those communicated to you? And could you give us a synopsis of what action you took with regard to this project upon assuming the position of chair?

Mr. Morrison: I was only aware on an anecdotal basis that there were issues — you know, press reports that I had been paying attention to for a few months before coming. Once I got to the office at the end of May, I began a process of, first of all, going through all the material that was available in the files, trying to get a picture back to the beginning of the project, how things got started, who the players were and who was involved. I instituted a series of management briefings where I was taken through from the very beginning, on a step-by-step basis, what happened. I spent a significant amount of time with the legal counsel, who was then involved in the process, trying to get up to speed on what we call the "referee process".

Just prior to me coming along in early May, the two companies, through legal counsel, had pulled together a referee process where this independent referee was brought on stream, and he was the arbiter of all activity between the two corporations in getting the project back to work.

The individual, Kim Dean, who was the referee, did an excellent job over time, in my opinion. He brought a lot of sound management of transmission lines to the project. He had a lot of expertise. The parties both listened to him, and he was able to help us get the project finalized.

In my process of going through everything, one of the very first things we did was — I think this would be September or so in 2003 by now — I asked for, and was finally given, some costs on the project. What I meant by costs was I think the board had been advised through the process that it was pretty close, or it was on track or off track, but nobody really had a very good handle on what the costs incurred in the project to that point in time were. I insisted on seeing that and was briefed by senior staff on those issues. We spent quite a bit of time debating whether all those costs were or weren't there and trying to find a way to get the local Yukon subcontractors paid.

Up until that point, and after getting through those early days and trying to see what the issues were, it became pretty clear to me by about October that we needed some help, that we needed an independent review of this project. Otherwise we were never going to make sense of it. I went to the board in October and we wrote to the Auditor General in late October, early November, I believe, to ask for the audit.

Mr. Cardiff: As chair of Yukon Energy Corporation, you would have worked closely with members of the board of directors. I'm just wondering, did any of the board members have expertise in electrical engineering or project management?

Mr. Morrison: No, and still don't.

Mr. Cardiff: Were any steps being taken to —

Mr. Morrison: Well, the board at that time had retained the services of a technical advisor, which is another way of handling the skills gap issue when you have a board of directors. You may have a board that doesn't have somebody with a good legal background, and you may need somebody to kind of help you through those things. In this case, the board had retained a technical advisor who had transmission line experience. What his role was, I'm not certain, because I wasn't there. He certainly — any time I asked him for advice — was very helpful and very knowledgeable, but I don't know how the board used the technical advisor through their process, and that's the kind of thing that isn't as evident — if you read the board minutes — as you might think.

Mr. Cardiff: Do you think it would be beneficial if that type of expertise were on the board?

Mr. Morrison: I think it would be helpful, but it would be helpful if we had a whole series of different experiences on the board. I don't think it's a necessity as long as the board deals with the skills gap in some manner. I can tell you that back in prior days with NCPC there was no expertise at that level, but when the Whitehorse Four Project was built there was an advisory group set up to advise the board that had the necessary skill levels, and that's another way of doing it.

Mr. Cardiff: With regard to the previous question, could we ask the board chair for his opinion on expertise at the board level?

Mr. Phelps: I essentially agree with what Mr. Morrison has said. It would be nice to have someone we could appoint who had some expertise. That would certainly be useful. But it seems to me that if you have a board that is proactive, they can get that type of expert advice from an independent person, and that was available to them. Whether or not they were really utilizing that expert properly is open to question. I just don't know.

But in my experience, as minister many years ago, we went through building the largest project in the history of YTG — the hospital — on budget and on time, and we relied very heavily on experts.

I think the problem here seems to somewhat mirror the problem that we discussed yesterday with regard to the board and the Energy Solutions Centre, and that is simply whether they were actively discharging their responsibilities and clearly understood them.

Mr. Cardiff: This question is again for Mr. Morrison and Mr. Phelps. We'd like to know whether or not the Yukon Energy Corporation has any plans to take on another major project in the near future, and if so, what steps are being taken to ensure that we don't run into these problems, both at the board and managerial levels in the future?

Mr. Morrison: The first answer is that there are no major projects planned for the immediate future. Having said that, we are moving both expeditiously and diligently to ensure our house is in order, and we are able to handle any projects that come before us — whether large or small — because if you can't do the small ones, you can't do the large ones. I think it's important that we have our house in order in that regard.

I talked yesterday quite a bit about new contracting and purchasing guidelines and spending authorities and signing authorities. Throughout the corporation, there's a very clear understanding now there are accountability levels, and people have to meet them. We've spent a great deal of time at the management level and we've spent a great deal of time at the staff level doing training and seminars internally on how these contracting and procurement guidelines work and what the responsibilities of all individuals are within the corporation — and I mean "all individuals". We've had everybody through these internal seminars and training programs.

If the board will agree, we're going to look at the project management end of things this year. I think we have a better project management system now, even in terms of planning and accountability. We have a committee rather than a department that looks at all the projects proposed for a year. They make the recommendations on the capital plan. We don't have a system whereby we're going to do anything as a separate project that's outside the normal day-to-day business. The planning and approvals for contract overages and extensions are diligently monitored so you don't get to spend more money on a contract without change orders. They're signed and approved ahead of time.

All these things were missing on the Mayo-Dawson project. It wasn't done that way. It was handled in a manner that didn't promote the best financial controls, the best control of the project nor an understanding of where things were going.

But I think we've taken a lot of steps. I want to take an extra minute, if you'll bear with me, and say that while we don't have any major projects planned, the greatest challenge facing the corporation into the future is that we very soon are going to run out of capacity in the system in terms of hydro supply. Growth in the system, as I mentioned a little bit I think yesterday, will necessitate us to look at where we're getting our generating capacity from in the future. So while we don't have anything planned, we are spending a great deal of effort in terms of infrastructure planning and will have options and will have processes for dealing with those options in the very near future. But we have to start looking. Electric energy supply takes a long time to put in place.

Mr. Phelps: If I could just add to that, one thing David left out was that we also proposed to involve the Yukon Utilities Board in projects that exceed $3 million in the future.

Mr. Cardiff: You mentioned that you are going to be dealing with a capacity problem in the near future, so there is some exploration of projects out there. Are you able to tell us what some of those options may be?

Mr. Phelps: Not at the moment, but I'm happy to do it at some later date. We have an internal infrastructure planning process underway. We're looking at the options, looking at the growth projections, and this is something that we will have to share on a public basis with the Yukon Utilities Board. We're not going to be going forward — I'm glad Mr. Phelps reminded me. We're not going to do major capital on a policy basis within the corporation. If we're going to build new capacity, we're going to the Utilities Board first.

Mr. Cardiff: I have just one more quick question. Earlier you mentioned the fact that in 1991, when the feasibility was done by both corporations, that this actually went before the Yukon Utilities Board, yet when the project proceeded in 2000, it wasn't, and it was felt it didn't need to.

Mr. Morrison: I'm not sure I can help you here. It's my guess that, back in 1991, the corporations were in a rate application process, and during that rate application process, as we are in right now — or now that we're before the Yukon Utilities Board — they filed their capital plans with the board. The board looked at the capital plan and said, "This Mayo-Dawson thing doesn't make any sense."

I don't know back then, so I don't want you to hold me to this, but I don't believe there was any requirement back then for the board to give that approval, but they probably provided comments. When management decided to go ahead in the year 2000, they specifically looked at whether or not this project had to be approved by the Yukon Utilities Board as part of the regulatory process. The conclusion they came to and the advice they then put forward was that there was no requirement for the project to receive the energy project certificate and therefore the approval of the Yukon Utilities Board.

I believe in the report the Auditor General has pointed out that was also the conclusion of the Yukon Utilities Board. The question, I believe — and I may be going a little further than you're asking — was, would it have been prudent to do it? I would suggest to you that it would have been very prudent to do it. Whether they had to do it or not is another issue.

Mr. Cardiff: Thank you.

Mr. Hardy: Yes. I was just thinking about that last answer, and it was one of the questions I was thinking of following up on, because it leaves something dangling out there.

Mr. Morrison: Well, let me give you my reasons for saying what I said. There's no requirement technically under the act — let's agree that there's no requirement technically under the act for the project to have received this energy project certificate. In other jurisdictions, they call it a certificate of public convenience. That applies in the electric utility business or the pipeline business or whatever it is. You're a regulated business. You're regulated by the Yukon Utilities Board. Before you can put costs that you incur into your rate base, you have to get the permission of the Yukon Utilities Board to do that. So even though the corporation didn't need to get permission to build it, they could never get permission to put it into the rate base until they go to the Yukon Utilities Board. So now you have a situation where you're taking the chance that you've gone ahead, built a project, and the Yukon Utilities Board could say to you, "You are not going to include that in rates." The Yukon Utilities Board looks at several issues. It looks at the costs and were they prudently incurred, and that's what they'll be doing on this one. But the Yukon Utilities Board also looks at the necessity to build the project.

I can give you an example. In Alberta, a number of years ago, there was a coal-fired generating plant built by an Alberta utility on the same basis. They didn't get approval first-hand. They went to the board after they built it, asked to put it into rates, and the utility board said, "No, you can put zero into rates." Well, that's the situation you're faced with. I think in this case there is a case to be built that there is a benefit of having the project, in the sense that there is a necessity for it. But how much of your costs are going in — when the Yukon Utilities Board reviews it up front, it says, "Yes, you can build the project, and this is the budget that we approve", because you have given them a budget. I think all of that brings a great deal of discipline to the process. So as I would have preferred — and my approach might have been different from what was taken. It wasn't wrong, but I think you're a lot safer if you do it the other way.

Mr. Phelps: If I could just add, Mr. Chair, looking at paragraph 33 of the Auditor General's report here, there is another reason, which may have been touched upon lightly. The board, in the process, would provide an independent assessment and critique of the proposed project which could lead to improvements in the project. So that's something they might have benefited from as well, had they gone before the board. So there are two reasons, the primary one being the one that has been discussed by David.

Mr. Hardy: It's almost a leap of faith when you describe it that way, and it's going back to that little saying that's used a lot now, "Build it and they will come."

The questions will now be handled by Mr. Rouble.

Mr. Rouble: Good morning, gentlemen, and thank you again for your participation in today's hearings, and thank you for your very candid and concise comments so far.

Due to the nature of the amount of this expenditure and the cost overruns, this is an issue that Yukoners — ratepayers and taxpayers — are taking very seriously, and they have many questions: how could something like this happen, why would it happen, and what are the impacts that will happen upon them, especially the impacts on ratepayers? Many of those questions we'll get to later — or the decisions, I understand, will be left up to the Yukon Utilities Board.

As is the Committee's practice, we pool our questions and divvy them up. I'm going to follow on with some feasibility and cost-benefit analysis questions. Right off the bat, Mr. Morrison, you just mentioned the necessity to build the project. I'd like to ask you to comment on that, and perhaps Mr. Phelps to comment on that as well.

Mr. Morrison: I think the necessity to build the project was driven by a couple of issues, and I'll give you my comments, as well, but let me go back. There's a surplus of hydro in the system: what can you do with it? It's dollars that are going by your door in one sense. You're generating that much power; the cost of generating that power is already being incurred, so can you use the power somewhere, because it'll provide some additional revenues. That's one way to look at it, and I think that was one of the issues the organization looked at at the time. The other one was: can we get Dawson off diesel? Diesels are noisy; they have greenhouse gas emissions and so on. The price of diesel fuel traditionally goes up; it's a non-renewable resource. If you can get a hydro project put in place, it's pretty static pricing. Pricing actually comes down over time. So you look at a project that way.

The big issue then becomes: can you do it economically? Is there an economic argument for going ahead? Even though it's a great idea, is it an economic argument? When the analysis was done, there was an economic argument that the price of fuel in 1998 — I think Eric told me this morning — was 29 cents. The economics was done at a little higher price of fuel than that, and it showed a cost savings over time of $14 million or $15 million initially, and I think we're talking about $20 million as the project goes along, and we've refined our numbers.

Did you need to do the project to serve Dawson? Dawson was already being served. You have to show a savings to the system over time, and the economics and the economic argument I've seen that was put forward at the time showed an economic benefit, but it's an economic benefit based on cost savings, not on the revenue stream you get from the ratepayers in Dawson.

Mr. Rouble: Were there any other factors in the decision to go ahead?

Mr. Morrison: I can't see any. I haven't seen any other issues in any of the material that I've looked at. Those were the key issues: getting the City of Dawson off diesel and providing some cost-savings over time, while finding a use for the surplus power in the Mayo system.

Mr. Rouble: What was the original project cost put forward by management?

Mr. Morrison: I guess if you talk about original — you're going to have to bear with me, in terms of searching my memory. I think it was in the $23-million to $25-million dollar range. You know, if you talk about original and we go all the way back to 1991, it was probably less than that, and I can certainly provide you with a chronology of costs. But over time the costs go up, as does the cost of fuel.

So, when I look at the Auditor General's report — you know, we were talking about $25 million in 2000, and then we crept up to $27 million, and then we crept up to $29 million, which was the final number approved by the board.

Mr. Rouble: So, when the board originally approved this project, what project cost did they approve, and were there any other conditions upon the approval?

Mr. Morrison: Yes, when the board approved the project in 2000, it was $27.2 million that they approved. That was subject to — I believe the number was a little different, but let me give you my estimate. I think there was a $4.8-million contribution from Yukon Development Corporation for a series of things, including the underbuild and some step-down connections along the route.

So Yukon Development Corporation was going to put forward a $4.8-million contribution — and also, flexible financing was going to be provided by Yukon Development Corporation that would save ratepayers harmless in the initial years when the cost of the transmission line project was greater than operating on diesel in Dawson. At that time, I believe it was expected to be about five or six years that the costs would be higher.

So this contribution from Yukon Development Corporation would make sure that ratepayers weren't paying any more.

Mr. Rouble: What other conditions on this project were agreed to by the board when the project was initially approved then? Were they involved in the decision to go with the design/build? Were there caps on it?

Mr. Morrison: The project was approved at $27.2 million. It was approved as a design/build contract as well. Those were the only other conditions. The cap at the time it was approved by the board was $27.2 million. That's what they approved as the expenditure for the project. Subsequent to that, management went back with a few items that they found that they had omitted, and the board approved the project expenditure going from $27.2 million up to $29.3 million or $29.4 million — roughly.

Mr. Rouble: Once the board gave approval, was that it? Could the corporation then go ahead with construction, or were additional approvals from higher levels in the hierarchy required?

Mr. Morrison: Once the board gave approval, the project could go ahead.

Mr. Rouble: Was there any ministerial approval of the project?

Mr. Morrison: There was ministerial approval in August of 2000, because the minister had to approve the go-ahead under the *Yukon Development Corporation Act* I believe.

Mr. Rouble: And what were the conditions upon the minister's approval?

Mr. Morrison: You're going to have to let me come back to you on that. I don't think there were. I think it was that the project could proceed. I'm not sure that the minister gave or had to give, but I'll have a look at it for you. I can't recall if there were conditions.

Mr. Rouble: Did the minister approve a specific dollar amount, or the design/build, or was it just, "Yes, go ahead and build this transmission line"?

Mr. Morrison: If you bear with me, maybe after lunch — I can't remember what the letter said, but if you can bear with me, maybe I can refresh my memory at lunch and try to provide a better answer.

Mr. Rouble: We would appreciate that. In retrospect, does management believe the $27.3 million or $29 million was a reasonable cost for this power line?

Mr. Morrison: I would think they did at the time. I mean, if they put the budget forward, I think they would have believed then that was what it was going to cost to build the line.

Mr. Rouble: The budget was reasonable?

Mr. Morrison: In hindsight, no. I think that's fairly evident when you go back and look at some of the comments the Auditor General has made and that Mr. Thompson pointed out this morning. The internal costs weren't — I mean, $1.2 million for internal costs, a great amount of which had already been spent before you even got started, wasn't reasonable. The optimism that was shown around the design/build agreement and design/build concept and how much time and effort that Yukon Energy Corporation was going to have to put into this didn't seem to be particularly well thought out at the time. In hindsight, it wasn't reasonable but at the time I'm sure they thought it was reasonable.

Mr. Rouble: At different levels of approval, was this optimism ever questioned?

Mr. Morrison: I think that's probably hard for me to answer. I don't know whether during meetings — certainly at the staff level, at the internal level, there would have been a number of meetings of a technical nature with the consultants and senior management staff. Whether they questioned those things, I haven't seen anything that would lead me to believe these issues either received a lot of scrutiny or didn't receive a lot of scrutiny. I can't help you there.

Mr. Rouble: In your earlier comment, you indicated that the original plan with a design/build project of this nature was that none of the staff were to be involved. We have already discussed that the internal cost increased from $1.825 million to about $8.3 million. I'd like to draw your attention to the chart on page 22. Perhaps you could walk us through this chart and explain the nature of the increases. It's a pretty significant factor in the overall cost overrun of the project.

Mr. Morrison: I'd be happy to do that, and I'll try not to editorialize. Project management fees went from an original budget of $150,000 to $2.5 million. This is the first line of the chart, and this, I think, points to the very significant issue of misunderstanding the design/build concept right from the very beginning. If you can picture this, in that I think the thinking was that the corporation was going to contract with some company that was going to basically be responsible for everything to do with the project, and it was going to take two years to build this. During that two-year period the corporation was going to hire an individual to be the project manager, which, in other terms, may be called an "owners' representative" or a "project manager" — a whole series of terms. That individual would represent the company's interest, so they would make sure that the contract was being followed, and that is pretty succinctly what a project manager's job is. It is to make sure that the deliverables are being adhered to, that approvals, where they're necessary, are given or not given, and they follow along with the contractor. Project managers exist on every job, territorial government capital projects or private enterprise ones. It's a pretty standard process.

I think the naïveté was that this was all it was going to take. I don't think that was a very realistic opinion at the time but, nonetheless, I believe it was the opinion of those involved in this. How they came to that, I don't know, but I can tell you that, as I mentioned to Mr. Cardiff, when I asked for an accounting when I got there and I saw a breakdown of the costs and saw the project management costs and where they had gotten to, I was pretty upset, to say the least. I still can't believe you can have that much of an increase in a budget.

The issues here are several. There were no controls. There was nobody controlling the expenditures of the project managers. This contract was an open-ended contract. That's how it got to $2.5 million. We talked about this yesterday. There were no limits on it; there were no caps on it. It wasn't being monitored or controlled by anyone and it just grew and grew. It grew because the project manager, all of a sudden, needed project engineering help.

The baffling part to me is that we had a company that was responsible for engineering. It's called design/build, and design/build means you engineer, you do the design and you engineer the project. Now we have a project manager and project engineers on the project. Where that may have been the understanding of the corporation where they thought they needed that additional help out there in order to make the project work, and there were things the contractor wasn't doing, I don't think anybody thought about whether or not the costs were prudent or had to be controlled.

It's also very difficult to understand how project engineering fits into a design/build contract.

So, my only thinking is that if I, as the owner's representative, felt that the contractor on the design/build part of it wasn't doing their job, I have a couple of choices. I can either stop the project, or stop the contractor at that point and ensure that he does comply with the terms of his contract and what his job is, or I can try and insert individuals into the process who are going to provide that kind of service to me. I think the decision was to add the project engineering, and I don't think it was a particularly great decision.

If you go down to the next one, I don't think the feasibility tender preparation — you know, there's a very significant increase of $100,000 over a period of a few years. We can see where the costs really haven't increased very much at all. Where we start to get into cost increases is there is a series of accounts — legal, contractors, consultants, insurance, materials, overhead and other — none of which were budgeted for, and, as the Auditor General has pointed out, all of which should have been budgeted for.

But I believe part of the reason they weren't budgeted for was an optimism, as I've said before, around the issue of design/build. The reason these expenditures began to occur was that it became clear that the design/build process wasn't going as well as it should have — trespass issues, rerouting and trying to get right-of-way and permits around rerouting around the airport.

I believe that the corporation reacted to these issues and these difficulties and began inserting resources into the process in order to mitigate these problems. That led to the increase in costs, and they're very significant.

If you look at this, this is all the increase in cost overbudget. There's a $7-million cost increase. The $7 million is right here — it's internal cost.

Mr. Rouble: Was there a deficiency in the original estimate, or did internal costs simply go too far beyond those expected?

Mr. Morrison: I think both. The initial estimate for internal cost was very optimistic, and I don't think very realistic either. When the project started having difficulties, internal costs started going up in order to compensate, to try to fix things and to try to deal with the issues. I don't think anybody anticipated having to deal with issues to this extent, so I think a bit of both.

Mr. Rouble: In the budgetary approval process, why wasn't this caught, and who didn't catch it?

Mr. Morrison: I can't answer you there. I can only say that this was a project that was primarily managed and run out of the president's office. When you have budgets and issues like this in terms of contracts, the item should have been caught. The board didn't catch it. Management should have caught this. It's just not realistic to go forward with a project of this size and those costs. I think they were very optimistic.

To be really clear, I think this misconception people had about the design/build agreement was a very significant issue in these costs not being caught. I don't think they understood what the involvement of the corporation was going to be so therefore thought it was pretty simple — these guys were just going to build it. I don't think that's great project planning.

Mr. Rouble: Who should be held accountable for these cost increases?

Mr. Morrison: I can say to you that none of the presidents that were involved in this are there today, and any of the staff that were directly involved aren't there. But the board should be held accountable because that's their job. I'm not sure what I can say to you. I understand your frustration, but a series of decisions were made and I think ultimately it's the board's responsibility to make the decisions for financial accountability. That's the only one I can point to.

Mr. Rouble: Was there a board champion or someone on the board who took a particular interest and followed this closely?

Mr. Morrison: Not as far as I can see.

Mr. Rouble: Let's see. In 2000, the corporation estimated that this project would produce savings of about $14 million. Has the corporation's estimate of savings changed since then?

Mr. Morrison: Yes, they have. They've gone up. I think today they're in the $20-million range, and that's primarily because the price of fuel has gone up. The price of fuel has doubled since 1998. It's 60 cents today.

Mr. Rouble: So this project is estimated to save $20 million?

Mr. Morrison: Over the life of the project, yes.

Mr. Rouble: What is the lifespan that is being used?

Mr. Morrison: 50 years.

Mr. Rouble: Reasonable and acknowledged lifespan for a wooden transmission line?

Mr. Morrison: Yes. Eric just reminds me that we have recently done a depreciation study, and that's what the depreciation study recommends as well. So we're consistent with that.

Mr. Rouble: Why was the capital cost to keep the diesel plant available as a standby operation not included in the original cost estimate? Is that a one-time capital cost, and what are the annual costs associated with that?

Mr. Morrison: I'm going to have to come back to you on the annual operating costs. I don't have them in front of me; I can certainly get them for you. The annual operating costs of the diesel plant on standby are not very significant, but I'm not sure I understand your question about the one-time capital costs of the diesel plant. Could you just help me a little bit with that? Perhaps just repeat it, Mr. Rouble.

Mr. Rouble: What was the capital cost to keep the diesel plant available as a standby operation, and why was that not included in the capital cost estimates?

Mr. Hoenisch: Included in the avoided costs of running diesel in Dawson is the fact that you eventually have to replace these diesels. If you don't run the diesels, they're obviously going to last a lot longer, so there is no new capital that you need to put in. There are some operating costs, which we can get you, but there are no new capital costs related to running the Dawson plant as a standby operation.

Mr. Rouble: Thank you.

Mr. Morrison, in August 2003, I believe that you told the board that the break-even point for the project was about $40 million, and the Auditor General suggested that the investment in this project could be justified if the capital cost did not exceed $38.2 million; however, in your press release of February 7, you suggested a break-even cost at about $52 million to $56 million. Could you explain the differences between these estimates, specifically between your estimate and the Auditor General's estimate?

Mr. Morrison: If you can just bear with me for a minute, I don't think it was me who said it was $40 million. I believe it was the president at the time.

Mr. Rouble: I stand corrected. It was the president in 2003.

Mr. Morrison: The difference between our estimates is — let me try to explain it this way. We are using a different methodology and different approach in terms of how we've estimated the economics of the line. We use a cost-savings approach. What we're saying is that the cost of the line is this, including operating the line over the period of time; the cost of fuel and operating a diesel system is this; and there's a difference of $20 million between what those costs are.

I believe the auditors are using, which is a very legitimate approach — I'm not suggesting anything from that. But their approach is that we have these costs and these revenues for the line, and there's the break-even point for that analysis of $38 million. It's a different analysis. It's not an analysis we use as a utility.

The big reason for that is — and I again come back to the point I made earlier, and I understand this is a little confusing — we don't have a Mayo-Dawson system as an isolated system. The revenues we get are for the entire system, not just Dawson City, so all our costs and revenues are pooled from all the different communities we serve and from all the different areas we provide service to.

We wouldn't normally look at it the way the auditors have looked at it, but it is a very legitimate economic analysis. It's just different.

Mr. Rouble: Well, I'm wondering which one you think is the more prudent factor to consider?

Mr. Morrison: We believe that our way of doing it is the right way to do it for a utility business. But let me say this, Mr. Rouble, and maybe help us with all of this. I don't think there is a point in me debating and saying I'm right or somebody else is wrong. We have an application in front of the Yukon Utilities Board. The Yukon Utilities Board will decide, on a utility and ratepayer basis, whether this project is economic or not, how much of this project will be included in our rate base, and what we are allowed to earn in terms of our overall rate of return.

I think the answer as to whether we've done our work appropriately or not will be something the Yukon Utilities Board will address, and I think it would be better to let them address it. We're debating utility economics, and I'm not sure that there is a benefit to that at this point.

Mr. Rouble: We're looking at this in the context of the feasibility, the cost-benefit analysis and the approval of the project. I recognize that the money is spent, and the line is in. I am concerned, though, that on one hand the Auditor General says, "This project makes sense if it costs less than $38.2 million." The utility, on the other hand, is saying, "No, it makes sense if it costs between $52 million, $56 million or $60 million."

Mr. Morrison: We are using different numbers and a different approach, and our numbers include fuel oil at 60 cents, not 35 cents. I think that's another difference. What I'm trying to say to you is that they're both right, depending on which approach you use. But we've not used a static number for fuel in our analysis, so I think there's a big difference there.

Mr. Rouble: The Auditor General's report, in paragraph 26, recommends that YEC should ensure that the scope and cost of capital projects are adequately defined and identified when seeking project approval. In your response to the recommendation, you say the corporation has recently improved its capital project process. Can you provide additional detail to your response, particularly with regard to how such a capital project process would have dealt with the problems experienced with the Mayo-Dawson transmission system project?

Mr. Morrison: The process that's in place today is a change from the previous system in this regard. All capital projects are now subject to two new substantive initiatives. First of all, the information requirements involved in putting forward a project are substantially more detailed and more rigorous than in previous days. So we now have a process called "project identification documents", so the initiating departments or engineering units can put a project forward but they have to complete a fairly detailed and very rigorous project identification document, which wasn't the case before. The information requirements for those were pretty limited.

Now, and also now, that project identification document goes before an interdepartmental committee which has representatives from the engineering or technical services department, the operations department and Finance. I think a big difference there is that we now have one of the senior managers from the Finance department involved in this process. That wasn't the situation before. So the project review committee does a rigorous analysis of all capital projects, whether or not the budgets are appropriate or not appropriate, whether the project is appropriate or not appropriate. It is then recommended up to the management committee. The management committee reviews all of these again to make sure that the appropriate budgeting has been looked at, and then it goes to the board. And that is a very significant change and improvement in the process from previous years.

In addition, I think I mentioned earlier, we're going to review that entire process and how we manage, then, each individual capital project to see if we're doing that in an appropriate and cost-effective manner. So we're trying to link the contracting and procurement audit that we've done to these changes in project approval systems and project management operations to make sure that we've got a very clear and well-defined system for doing all these things.

Mr. Rouble: I would expect, then, that many of these internal costs are being factored into these new capital costs.

Mr. Morrison: We factor internal cost, and again, Eric is going to have to remind me of the terminology.

Mr. Hoenisch: Engineering, support and general costs, kind of a general overhead, are added to projects.

Mr. Rouble: So that's what management is doing, then. Mr. Phelps, what is the board doing, then, to increase its scrutiny of capital cost projects that come to it for approval?

Mr. Phelps: Well, what we would do — do you want to go first?

Mr. Morrison: Yes. Can I just add a piece for Mr. Phelps, given his recent appointment. The board process change that is there and has been implemented just before Mr. Phelps came along is that when that — not only does the board get the approval of the project budget, but the board is provided with a review on a quarterly basis of all capital projects, the status of all capital projects, the amount of money spent to date on a capital project, where that project is to budget, where we think the project is going to end by year-end — is it going to be completed on budget, on time, is it not going to be, what are the difficulties if there are any? And the board has been getting a rigorous review of that.

If there are projects that are, because of — and let me give you an example. We do a budget for an overhaul of a hydro unit. They're very, very difficult to budget because, very simply, we can identify the problem of the overhaul or the requirement for it, but when you start taking a piece of machinery apart you often find other problems.

So any costs additional to budget are brought back to the board for approval prior to expenditure wherever possible.

The board has a more rigorous process in place. This wasn't happening prior to the last year and a half or so. So that system is very rigorous, and the board has the ability now to be aware of issues around all capital projects. These are not major projects. These are projects that might be $50,000 and up. But anything of any significance is in front of that board. There is also a quarterly report that goes to the board — a written report as well as an oral presentation by the director of technical services.

Mr. Phelps: I was just going to say — and all these things are correct — that were it to be a significant capital project, and if the board were to have any concerns at the outset, we wouldn't hesitate to bring in outside expertise to help us examine the project right at the start.

Mr. Rouble: I'm glad to hear that steps are being taken to improve the scrutiny at all levels. I would like now to turn back to the project and look at the overall project management to find out what the level of scrutiny was when the project was going on. What was management's role in identifying cost overruns? How were those communicated to the board? How were they approved?

Mr. Morrison: As much as I'd like to tell you, Mr. Rouble, that there was a system in place for all that, I don't believe there was. Management's involvement in the project was — the president was reporting to the board on the project. The reports were — I'm trying to search for the word — anecdotal or editorial in nature. They were verbal. They were written, but they were words. There was no board approval of these cost overruns that you've seen.

The board approved a budget of $29 million. That was the last time the board approved expenditures on the project. They weren't being brought back to the board for approval. As I said, the board was being told about the project and the progress and that there were difficulties with the contractor and there were issues, but they were written reports that were narrative in nature — that's the word I'm looking for — rather than very specific, detailed, budgetary reviews at the board level. It didn't happen.

Mr. Rouble: Did the board not question if we are on budget or not?

Mr. Morrison: I believe the board asked if we are on budget and they were told no, either close or pretty close, looking like it's going to be on budget or maybe we're having a problem, but it was narrative. Nobody provided — I understand that you're astounded by this — a detailed financial accounting of the project between the time it was approved and when I asked for one when I got there, in the summer of 2000.

Mr. Rouble: Were board members satisfied with that?

Mr. Morrison: I can't answer that.

Mr. Rouble: As the minister was also involved in the approval of this project, were there regular updates at the ministerial level?

Mr. Morrison: I can't answer that. I don't know if there were or weren't. As I said earlier, there's nothing I've seen. In the board process, if we do things, we provide information to the board, we provide copies, but I don't see anything in that regard. I haven't seen it, anyway.

Mr. Rouble: So, once the minister signed off on this project, that was the last of the communication or accountability?

Mr. Morrison: I don't know that, Mr. Rouble. The chair or the president may have met with the minister. I don't know.

Mr. Rouble: Were there any written updates?

Mr. Morrison: Not that I'm aware of. I'm happy to have a look at it, but not that I'm aware of.

Mr. Rouble: I think we would all appreciate if you could find if there were written updates.

Mr. Morrison: Like I said, I haven't seen any.

Mr. Rouble: In its report, the Auditor General says that management did not follow basic project management principles. Is there any explanation why this happened?

Mr. Morrison: I'm not sure that I can give you an explanation. I can maybe give you my thoughts as to why I think these things happened.

For some reason, there seemed to be an urgency. I can't document it for you; I can't point my finger to it, other than it's apparent to me — when you look at how decisions were made and when they were made — there seemed to be an urgency to do this project. Somebody had an urgency. I don't see it at the board level; I can only see it at the management level. There was a push to do it.

During the period of time that Mr. Robinson was there in the president's job, there were decisions to go ahead and some of those issues around that, and some of the questions you may have today surrounding that decision to go ahead, are pointed out in the auditor's report.

It doesn't make a lot of sense to me from a business management or a management point of view as to why you would run this project differently than you would any other business transaction. I don't understand it. The project was clearly separated from the day-to-day business of the corporation. It was supposed to be handled by the project manager, reporting most of the time to the president. There were individuals within the corporation who were asked to go out and help in different capacities for short periods of time, in and out of the project. I don't understand the approach but, once started, it seems to me that the momentum of the project dragged everybody along in wanting to get it finished, with nobody actually stopping and asking, "Are costs are in line? Are we doing the right thing here?" It seemed to take on a momentum of its own, and I can't explain it.

Mr. Rouble: I can appreciate the momentum of the project, but to have internal costs increase from $1.8 million to almost $8.3 million — I just find it incredible that no one recognized these costs and no one asked about them.

Mr. Morrison: I do, as well. I have no argument with you on that. I was clearly upset when I began to realize where these costs were and that nobody was reporting them. But nobody was reporting them up for a very good reason. I can tell you that when I showed the board where we were in August 2003, they were also very, very concerned. But up until that point in time, nobody had given them a number, and nobody had outlined what that number was comprised of.

Mr. Rouble: Obviously, the spending limit authorized was exceeded.

Mr. Morrison: Well, you can look at that a couple of different ways. And the reason I say this — and this is, I think — and I'm glad you've brought me to this, because I'm trying to search for some answers for you, and I'm not sure I have them in all cases. But one of the problems with spending authorities that we've recognized is that management got a $29-million budget approval. The signing authority limits that existed then and to a certain extent exist today are that the president could approve capital expenditures up to $1 million. I believe that the excess or what was transgressed here was that you could approve capital expenditures up to $1 million once the budget has been approved. I believe that people looked at that and said, "Well, I can approve capital expenditures up to $1 million or operation and maintenance expenditures up to half a million dollars," and forgot the part about, well, where's the budget approval. Because once you've passed the $29-million mark, you didn't have any authority to spend any money.

At least, from my point of view, somebody needed to say, "Excuse me. We think we need $2 million or $3 million more here. Would you give us a budget approval to increase the budget from $29 million to $30 million, $31 million or $32 million?"

So, I think there was a misjudgement, or a misapplication, of what spending authorities really mean. Now, it translated out into the project. There is a process — and a well understood process in project management, or in operational or capital budgeting — that if you anticipate additional costs, you either get a change directive signed and agreed to by the parties or you get a change order signed and agreed to by the parties.

There should have been no difference to that for the overall project budget. If management was going to exceed the $29 million, they should have brought a change order to the board and requested approval of that change order for an increase in the budget. But it didn't happen.

Mr. Rouble: Mr. Chair, that's the extent of my questions for right now.

Mr. Hardy: Yes, thank you for struggling through this period. There will be a lot more questions, I believe, as we try to sort it out.

You have indicated, Mr. Morrison, that during the break you will try to look through some of the notes and minutes, et cetera. We'd really appreciate that because we'll probably come back to some of these questions, and if you have that, we'd appreciate it.

Mr. Morrison: Yes, I'll do that over the lunch break.

Mr. Hardy: Thank you very much.

We have approximately 15 minutes left. I'm going to turn the questioning over to Mr. Cathers.

Mr. Cathers: Thank you, gentlemen, for appearing before us today.

I'd like to turn the attention at this point to the contracting practices of the corporation. During this project, the corporation awarded 12 contracts over $50,000 each, without competition. Can you explain why these contracts were sole-sourced, and if there was a valid reason for doing so?

Mr. Morrison: Well, I can't tell you what their thinking was, but I can tell you what I think happened. My belief is that, by this time — not the mood, but the concerns about the project that were being experienced within the organization led to individuals making decisions that were reactive.

In other words, they were reacting to things and, when you react to things without thinking and planning, you tend to want to fix things or resolve issues as quickly and easily as possible — not always the most economically or the best way to do it.

I think it was in reaction to trying to solve issues, and the contractors were either known or were people they had experience with or businesses that had some relationship at some point in time with the corporation, so it was easy to sole-source.

The contracting and procurement practices of the corporation at the time also permitted this, because there was no real system in place to provide good reasons for sole-sourcing. People could just go out and contract with people. There was no system of checks and balances. We've instituted a new system; we have those checks and balances today. I'm sure you're tired of hearing me say that sole-source contracts have to come to my desk for approval; they have to have good reasons. You just can't go out and do these things.

At the time, it was the nature and the culture. It could happen and it did happen.

Mr. Cathers: Thank you for that. I guess that's as good an explanation of the rationale behind the decision of the time as we can ever hope to get. It's a little bit baffling, looking at some of these things we see were done.

Can you explain — again, asking you to look somewhat back into the past as to why it appears that decisions were made — why the corporation opted to negotiate with the only valid bidder on the original tender rather than retender the construction contract, and why the corporation did not retender the contract when concerns came to light about the construction contractor's lack of experience and about problems with the proposal?

Mr. Morrison: I'll try to give you what, in hindsight, is my understanding of what happened and why.

The system — the corporation at that time and, in some instances, today and on this particular project, employed a two-envelope system. The two-envelope system is an option that is out there in the contracting world, and its main purpose is to ensure that you get a very objective review of potential bidders and that, if you have a bidder and you look at their bid and they have some weaknesses but their price is good, you don't get the capacities and the capabilities of the individuals mixed up with their pricing.

In this case, I think the worst of all possibilities occurred. We had three bidders on the project. Two of the bidders were very experienced in not only the transmission-line construction line but in the overall utility construction business. They looked at the contract and they put their bids forward, and the process for reviewing all of the bids meant that you opened the proposal first, the design/build proposal, and then, if the contractor qualified under the conditions of the tender with all of the conditions in their proposal, then you would look at the price.

Unfortunately with, again, an inexperienced corporation from a design/build point of view, the tender documents were sent out and three people responded. Now, there were quite a few people who had been shortlisted, but only three responded. The two corporations that had a lot of experience both indicated in their proposal that there were some issues around the contract and there would have to be some discussions about those issues before they were prepared to go forward.

From an information point of view, the contract is very, very large — volumes and volumes. All bidders were provided with a copy of the contract they would potentially have to sign.

Based on their response, the two bidders were immediately disqualified, and their price envelopes were never opened. They were returned to them, so we don't know what their price was.

When the corporation sat down — after looking at Chant's proposal and agreeing that it met the terms and conditions, they opened the price envelope. After scrutinizing the proposal, it was evident there were some very great issues and, quite frankly, Chant hadn't been ranked very high on the list of potential bidders when we did the shortlist. There were some issues around their experience — substantive issues.

There was an opportunity, because of the pricing issues — as I understand it, they hadn't met all the conditions of the pricing side of things — to walk away, to say, "We're going to retender this." I can't tell you what people's minds were doing at the time, but the decision was made. As I said earlier, there was this feeling that you had to do this, that this project was something that had to get done, and retendering would have meant losing — I believe the timing was that retendering would have meant you would have been into the next year before you would have been able to start work on this project, so you would have lost the year because of it getting into winter and work that had to be done and things like that.

So the decision was to negotiate with Chant, to get some clarity around these issues and get some agreement on how they could be dealt with.

Hindsight is 20/20, and particularly in this case. There was some vague reference that legal advisors indicated that there may be some issues if they didn't go forward, but I think those issues could have been dealt with. The opportunity was there to walk away. They didn't and decided that they could live with what they thought were Chant's inadequacies in terms of experience. I don't understand the rationale behind that, because never having built a transmission line previously — you know, it should have been a pretty significant signal to someone that they needed to step back and re-examine things. So I can't speak for what their thinking was, but my understanding is that they didn't want to lose the season so they thought they'd go ahead.

Mr. Cathers: Can you tell whether any consideration was given to the fact or even awareness taken of the fact that the two bidders who had expressed concerns with whether the contract was workable as it was worded were very experienced companies and that perhaps they should take a second look at if there were flaws in their contract?

Mr. Morrison: From what I can determine, and from reviewing that, that didn't send enough of a signal to anybody. They didn't put as much onus on that as they perhaps should have, in hindsight. That would have sent a very clear message, maybe, to more experienced individuals, but it didn't send a message to them. I think, again, at the time that this was happening, the individual who was the president had experience in design/build contracts and that may have been the thought that he felt he could deal with it — you know, he could deal with these issues. I can't suggest anything other than that. But I don't think there was a lot of onus put on the fact that because you have experienced people telling you there is a problem you need to step back.

Mr. Cathers: You referred to — I believe your term was "a sense of urgency," or at least a sense that this project simply had to happen. Is there any indication of where this sense of urgency came from? Was it at the board level? The management level? Ministerial direction?

Mr. Morrison: I think it was at the management level. I don't see anything to indicate that the board really pushed the project at all. It certainly reviewed and approved it when it was brought forward by management, but there was no driver from the board side. And I don't see anything from the minister's side.

Mr. Cathers: This sense of urgency seems to be something that, from what you're saying, is continuing through all these steps — this turnover of management, on and on and the drive toward whatever that end might be.

Mr. Morrison: The only thing that logically drives that is that the sooner you have the project built, the sooner you start saving money. But is that a significant enough amount of money in the short term to justify going ahead on a project when you're not ready? That doesn't make sense to me. That doesn't balance. I'm just trying to think of reasons why people might want to do those things.

Mr.??Cathers: In your response to questions from Mr. Rouble earlier, you referred to somewhat narrative updates to the board by management, and that there was a lack of a record — at least, that you've been able to find — of how frequently meetings took place between the chair of the board and the minister and whether those updates were occurring or not.

Can you tell whether approval was sought from the minister responsible for the corporation to follow the procedure of not retendering the construction contract, but instead to negotiate it with the successful contractor, or whether the minister was even made aware of that?

Mr. Morrison: I don't believe that anybody tried to obtain the minister's approval for that. I don't see anything that indicates that or whether the minister was made aware of that. No, I don't think that happened.

Mr. Cathers: It sounds like this is a case of a real lack of a paper trail and that, from what you're saying, there's a lack of evidence of whether or not updates were given to the minister on the project and whether or not that was in writing. Is there any evidence of the minister, at any point, demanding that there be written updates or an accounting throughout this process, or was it just going along?

Mr. Morrison: I'm not aware that there were written requests for updates, so I don't know what the communication between the chair and the minister was.

Mr. Cathers: Moving on to the next area —

Mr. Hardy: Mr. Cathers, you're just going to start another line of questioning, and it is 12:00.

Seeing that it's 12:00, I'll stop the proceedings and we'll reconvene at 1:30. I'd like to thank you for this morning's session.

Recess