

January 31, 2008

Mr. Joe Acorn, Chairman
NWT Public Utilities Board
#203-62 Woodland Drive
Hay River, NT
X0E 1G1

Dear Mr. Acorn,

Re: NTPC 2006/08 GRA – Code of Conduct

In Board Decision 17-2007, the Board issued the following Directives to NTPC:

49. The Board directs NTPC, by the end of January 2008, to file with the Board a formalized inter-affiliate code of conduct which would establish principles related to pricing and other matters governing all transactions with the Corporation's parent, other affiliates and non-regulated operations.
50. The Board directs NTPC, by the end of November 2007, to file with the Board a detailed policy that explains how the interests of the regulated ratepayers will be protected in relation to decisions by the Board and Senior Management regarding the operations of NTPC and NTHC. In particular, the Board expects a detailed explanation as to how it will be decided which of the two companies will pursue new generation and sales opportunities and how the interests of the regulated ratepayers will be protected in that decision-making process.

On November 30, 2007 the Corporation filed with the Board and served on Interested Parties its draft Policy No. A-3 "Guidelines for Regulated versus Non-Regulated Business Activities" in satisfaction of Directive No. 50. That policy sets out the factors which shall be considered by the Boards of Directors and management, including the overarching legal and fiduciary duties owned to each company, when determining which business opportunity should be undertaken by which entity. The policy was approved by the Corporation's Board of Directors on January 22, 2008 and is incorporated into the NTPC Code of Conduct.

By this letter, the Corporation is filing its "Code of Conduct for Affiliate Transactions" in response to Directive No. 49 (the "NTPC Code of Conduct"). A copy of this filing has also been served on all Interested Parties on the Corporation's 2006/07 and 2007/08 Phase I GRA service list. A copy of the NTPC Code of Conduct is attached to this letter as Appendix "A".

DEVELOPING THE NTPC CODE OF CONDUCT

The fundamental goal for the Corporation in developing the NTPC Code of Conduct was to address the concerns noted by the Board in Decision 17-2007 in a manner that also accounted for the Corporation's operating environment, which currently involves a limited competitive environment, small volume and value of inter-affiliate transactions and limited available resources that are ultimately paid for by its customers. To that end, the Corporation reviewed:

- Decision 17-2007;
- the *Northwest Territories Hydro Corporation Act*, the *Northwest Territories Power Corporation Act* and the *Public Utilities Act*;
- the ATCO Code as approved in EUB Decision 2003-040 (Affiliate Transactions and Code of Conduct Proceeding Part B: Code of Conduct);
- the cost tracking measures employed by other Crown utilities, namely Newfoundland and Labrador Hydro and Manitoba Hydro; and
- the cost tracking measures currently employed by the Corporation.

The Corporation determined that simply adopting a code of conduct, albeit with modifications, developed and approved for another utility operating and regulated in another jurisdiction would simply not meet the above fundamental goal. Rather, a "made in the NWT" approach was required. Therefore, NTPC Code of Conduct must be appropriate for the Corporation and the transactions it engages in with its affiliates. The NTPC Code of Conduct must also comply with the legislatively established structure of the electric utility industry in the Northwest Territories.

The NTPC Code of Conduct attempts to minimize costs ultimately paid by customers through rates by focusing on inter-affiliate cost tracking and information retention requirements. Such information will be will provided to the Board and Interested Parties so that they may periodically assess the relatively small number of inter-affiliate transactions engaged in by the Corporation, including joint-use facilities, and satisfy themselves that ratepayers are indeed not harmed by such transactions.

The NTPC Code of Conduct is a flexible document that can easily be modified in the future to address other types of inter-affiliate transactions or requirements that do not presently arise. The Corporation expects that should the type, degree or volume of its inter-affiliate transactions become more complex, it will amend the NTPC Code of Conduct as required.

Sincerely,



Judith Goucher, Director, Finance & CFO

cc: Interested Parties

APPENDIX “A”

NORTHWEST TERRITORIES POWER CORPORATION CODE OF CONDUCT FOR AFFILIATE TRANSACTIONS

This Code of Conduct will be applied in conjunction with the following Policy: *Guidelines for Regulated versus Non-regulated Business Activities* which was filed with the PUB at the end of November 2007.

Policy:

The Boards and management of the Northwest Territories Hydro Corporation (NT Hydro) and the Northwest Territories Power Corporation (NTPC) will conduct business and make decisions based on the highest ethical and professional standards and minimize any potential for conflict of interest. In particular, the Boards and management shall conduct business and make decisions in a manner which considers and safeguards the interests of each corporation. Inter-affiliate activity and transactions shall be transparent and adhere to applicable inter-affiliate generally accepted accounting principles and NTPC's inter-affiliate code of conduct as approved by the Public Utilities Board (PUB).

Background:

Section 4(3) of the *Northwest Territories Power Corporation Act (NTPC Act)* provides that NT Hydro owns the common (voting) shares of NTPC making the NTPC a subsidiary of NT Hydro. Section 8(1) of the *Northwest Territories Hydro Corporation Act (NT Hydro Act)* provides that the Board of Directors of the Northwest Territories Power Corporation is designated as the Board of Directors of the NWT Hydro Corporation. Similarly, Section 13(1) of the *NT Hydro Act* designates the President of NTPC as the President of NT Hydro. Several other of NT Hydro's indirect subsidiaries share the same Board of Directors and have overlapping management as NT Hydro and NTPC.

Common directors and officers of the parent company (NT Hydro) and its subsidiaries (NTPC, NWT Energy Corporation (03) Ltd., Sahdae Energy Ltd. and others) must always be cognizant of, and act appropriately with respect to their fiduciary duties owed to each entity. Case law and best practices require, “[d]irectors, in each case, to act in the best interests of the relevant company. When making decisions for the subsidiary the directors must act in the best interests of the subsidiary. They must not set aside the

subsidiary's interests for the parent's agenda".¹ The same best practices also apply to common officers.

Section 76(1) of the *Public Utilities Act* requires that "[a] public utility shall provide safe, adequate and proper service and keep and maintain its property and equipment so that the public utility can provide the service." The *NTPC Act* and the *NT Hydro Act* establish the objects of NTPC and NT Hydro, respectively, to generate, transform, transmit, distribute, deliver, sell and supply electricity on a safe, economic, efficient and reliable basis.

The combined requirements of the foregoing provisions impose a "quality of service" obligation on both NTPC and NT Hydro that must also be adhered to by the respective Boards of Directors and management.

It is also recognized that the PUB may review and approve costs incurred by and charges for service levied by any public utility falling under its jurisdiction that is not otherwise declared to be exempt by PUB order or excepted by statute.

Other sources of requirements governing the Boards of Directors and management include the *Conflict of Interest Act*, the *Financial Administration Act*, the *Access to Information and Privacy Act* and the *Public Service Act*, as well as directions issued from time to time by the Executive Council pursuant to Section 8(4) of the *NTPC Act* and Section 9(2) of the *NT Hydro Act*.

Directives:

The following factors shall be considered by the Boards of Directors and management when determining what is in the best interests, in each case, of the parent and its subsidiaries, and what best meets its quality of service obligations, when determining which business activities should be undertaken by which entity.

1. Risk

Every business venture or activity contains an element of risk. Risk must be proactively identified and managed. Each corporate entity may have different risk tolerance. Generally, if a project/activity risk is high and the potential for downside to regulated rate payers significant, then the project/activity should be undertaken in a manner and by an entity that will not expose the regulated customers to a liability or cost should the project/activity be unsuccessful.

¹ STP Director's Liability in Canada – Liabilities Relating to Corporate Law, page 1-55

2. Legal Restrictions

If a corporate entity is legally restricted in legislation, its constituting documents or any directions or policy guidelines that may from time to time be issued or established by the GNWT Executive Council from certain types of operations or business ventures (i.e. joint ventures or debt limits/guarantee restrictions), then the project would not be undertaken by that entity.

3. Confluence

Where a project will likely converge with operations that serve regulated ratepayers, then the project/activity may be undertaken by the entity serving those ratepayers (i.e. the project would be ultimately required to serve regulated customers and it is being advanced or expanded as a result of that opportunity).

4. Divergence

Where a project/activity diverges from or is unrelated to current or foreseeable service to regulated ratepayers, then such project/activity would be a candidate to be undertaken by a corporate entity that does not serve regulated ratepayers.

5. Access

Where a corporate entity serving regulated ratepayers does not have access to a particular business opportunity but another corporate entity not serving regulated ratepayers does, then the project/activity would be undertaken by the entity that could access the opportunity. For example, federal funding contributions often have conditions that cannot be met by a Crown corporation or regulated entity. Similarly, a joint venture partner may not be willing to do business in a manner that results in regulation of it or its investment.

6. Leverage and Majority Position

In cases where a project/activity requires extensive third party equity, joint venture partners, or other forms of financing, such that the entity serving regulated ratepayers is not in a majority (control) position, then it may be necessary to pursue the project/activity through a corporate entity not serving regulated ratepayers.

7. Project Permit

In the event a project/activity is intended to be pursued by the entity serving regulated ratepayers, but a project permit is denied by the

PUB, the project/activity may then be pursued by an entity not serving regulated ratepayers.

8. Transparency

In addition to the foregoing factors, the following principles will guide NT Hydro and its subsidiaries with respect to inter-affiliate transactions:

- i. All inter-affiliate transactions shall be fully transparent and compliant with NTPC's inter-affiliate code of conduct as approved by the PUB.
- ii. It is understood that NT Hydro and its subsidiaries shall have the right to manage their affairs but accept that the regulated operations must demonstrate to the satisfaction of the PUB that all inter-affiliate transactions involving regulated operations are prudent and compliant with NTPC's inter-affiliate code of conduct as approved by the PUB.

NTPC AFFILIATE TRANSACTIONS

In 1988 the Northwest Territories Power Corporation ("NTPC") was established by legislation as a Crown corporation of the Government of the Northwest Territories.

The Northwest Territories Hydro Corporation ("NT Hydro") was established by legislation on June 30, 2007. The attached organizational chart outlines the current corporate structure of NT Hydro and its subsidiaries.

Under the new structure, NT Hydro wholly owns:

- NTPC;
- NWT Energy Corporation (03) Ltd. ("NTEC(03)"); and,
- Sahdae Energy Ltd. ("Sahdae").

NTPC wholly owns:

- NWT Energy Corporation ("NTEC"); and,
- 5383 NWT Ltd.

The nature and scope of the non-utility operations conducted by the above subsidiaries are as follows:

- NTEC, under the authority of the Northwest Territories Power Corporation Act, financed the Dogrib Power Corporation in 1996 for the construction of a 4.3 MW hydro facility. NTEC also has responsibility for the operation, management and 50 percent shared ownership of one residual heat project in Fort McPherson.
- 5383 NWT Ltd. is an inactive company.
- NTEC(03) has two operations: the development of business opportunities outside the regulated business including development of hydroelectric projects and a one-third investment in Deze Energy Corporation Ltd. a company involved in the expansion of the Taltson hydro system, started in 2006. At the present time, NTEC(03) has two employees, who are on secondment from NTPC. All salary, benefit and expenses related to the activity of these two employees are directly charged to NTEC(03).
- Sahdae began operations in 2005. Its mandate is to pursue a hydro development project on the Great Bear River to provide power to the potential Mackenzie Valley pipeline. Activity in Sahdae has consisted primarily of community education regarding the potential hydro project and participation in the Mackenzie Valley Pipeline regulatory hearing process. The limited activity that has taken place to date has been delivered by NTEC(03) employees.

At the present time and for the foreseeable future, NTPC's affiliate transactions involve sharing of financial reporting, purchasing, IT support and senior management services with NTEC, NTEC(03) and Sahdae. The ability to share costs with affiliates presents an opportunity for the regulated customer that would not otherwise be present. If the provision of services to affiliates gives rise to incremental costs, all of those costs will be directly charged to the affiliate and/or NTPC will advise its affiliates to engage those services from other parties.

In sharing such services, NTPC will attempt to maximize the utilization of its utility resources and recover a component of the costs (on a cost recovery basis) to the benefit of ratepayers. As discussed below, such shared services are appropriately allocated to the Corporation and its affiliates by direct charges or overhead allocations.

The onus is on NTPC, the regulated utility, to provide evidence in support of the inter-affiliate transactions.

AFFILIATE COST TRACKING

The foundation for transparency of inter-affiliate transactions is the documentation of transactions and the ability to provide evidence in support of the assumptions. NTPC already has a system in place to facilitate the review of inter-affiliate transactions and will implement further steps to improve

documentation of transactions and enhance inter-affiliate transparency, fairness and senior management accountability with respect to inter-affiliate transactions impacting regulated business.

For cost tracking purposes, different plant numbers are established for each of the subsidiaries to identify transactions related to non-regulated companies. Different plant numbers for each community and head office are also in place to track the regulated operations of the Corporation. For capital assets or long term projects undertaken by the non-regulated subsidiaries, specific project accounts are set up to separate these costs from regulated operations, as well as non-regulated operational expenses.

There are two ways in which costs are allocated to non-regulated operations:

1. **Direct charge** – time and supplies are directly coded to the non-regulated plants for those costs that are readily identifiable as non-regulated transactions. This would include such costs as:
 - a. direct employees whose salaries and benefits are separated from the regulated operations and directly charged to the non-regulated operations via timesheets;
 - b. time spent to build assets or perform operational services on a periodic basis for the non-regulated operations – these costs would be charged through timesheets;
 - c. interest expenses on debt held by the non-regulated operations;
 - d. daily operational costs (i.e. rent, office supplies, hiring costs, advertising, etc.) for non-regulated operations are directly charged to the appropriate plant through service agreements or purchase orders; and
 - e. travel is itemized and coded using travel claims.
2. **Overhead allocations** – for costs that are incurred in small increments or are not readily identifiable as non-regulated transactions, the Corporation applies an overhead allocation from regulated operations to non-regulated operations. This overhead allocation is reviewed on a quarterly basis to ensure the rates are applicable for the non-regulated activity expected each year. This would include such costs as time for financial reporting, purchasing and IT spent on producing financial statements, purchasing supplies and maintaining computers for the non-regulated operations.

To provide sufficient transparency to allow for testing of inter-affiliate transactions, NTPC will develop the following:

- Annual description of inter-affiliate transactions, which will form the basis for the annual budget for NTPC to provide inter-affiliate services. The budget will show as an offset to regulated costs and will be disclosed in sufficient detail to allow for testing against assumptions of services and assets to be provided;
- Internal quarterly reports on inter-affiliate transactions and costs incurred in the provision of services and assets to affiliates and annual reports which will be filed with the PUB as part of any future general rate applications; and
- For the foreseeable future, it is not contemplated that NTPC would receive services from affiliates, however if that were to change, a similar process would be established to track the receipt of services and assets provided by non-regulated affiliates and the corresponding cost incurred and this code will be updated.

Northwest Territories Hydro Organization Chart

