

## **COSTING OF WORK**

### **1.0 OVERVIEW**

Hydro One Distribution's work program is bundled into packages of work identified as programs or projects. Program and project costs are comprised primarily of activities associated with labour, equipment and material acquisition. This Exhibit details the breakdown of each of these three cost activities, and how the costs are applied to programs and projects. This costing approach is consistent with the requirements of Generally Accepted Accounting Principles ("GAAP").

Hydro One Distribution categorizes its costs into two major classifications - common and direct. Common costs, both OM&A and capital expenditures, are allocated to Distribution and Hydro One's other lines of business. Direct costs charged to work orders include labour (comprising salaries, benefits and pension costs), material, fleet and supply chain. Labour costs are calculated as a product of actual time multiplied by the standard labour rate. Material costs are charged directly to the work program. Fleet costs are charged using a fleet rate, and supply chain costs are charged via a material surcharge. All of these elements are described in detail in this Exhibit.

### **2.0 PROJECT AND PROGRAM MAJOR COST CATEGORIES**

#### **2.1 Labour Rate**

Trade labour and equipment hours are distributed directly to benefiting programs and projects by using timesheets, consistent with common industry practice. Standard hourly labour and equipment rates are then used to convert the reported hours into costs. Both labour and equipment rates are "fully loaded" to ensure that all associated support costs

1 required to deploy resources and equipment are accurately and cost effectively distributed  
 2 to the benefiting work.

3  
 4 On an annual basis, the standard labour rates are derived based on information gathered  
 5 through the annual budgeting process. Resource budgets for each major resource  
 6 category are calculated and categorized into three basic cost components: forecast  
 7 billable (direct charged) hours, forecast non-billable hours and forecast non-billable  
 8 expenses. Total payroll and expense costs along with an assignment of support activity  
 9 costs, divided by the forecast billable hours, create the standard labour rate. Table 1,  
 10 below, shows the composition of the standard labour rate for a Regional Line Maintainer  
 11 – Regular Staff, over the period 2006 to 2011.

12  
 13 **Table 1**  
 14 **Standard Labour Rate Composition**  
 15 **Regional Line Maintainer – Regular Staff**  
 16

	Historic			Bridge	Test	Test
	2006	2007	2008	2009	2010	2011
Payroll Obligations	<b>60.22</b>	<b>60.98</b>	<b>61.42</b>	<b>57.83</b>	<b>61.78</b>	<b>63.66</b>
Contractual time away from work	14.42	14.47	14.93	14.29	15.20	15.70
Time not directly benefiting a specific Program or Project	7.70	8.27	9.95	10.37	10.08	10.42
Field Supervision and Technical Support	2.80	9.07	11.08	13.04	8.54	8.67
Support Activities	10.35	10.71	13.61	13.47	14.40	14.55
<b>Labour Rate</b>	<b>95.50</b>	<b>103.50</b>	<b>111.00</b>	<b>109.00</b>	<b>110.00</b>	<b>113.00</b>

17  
 18 The cost elements embedded in the standard rate as illustrated in Table 1 are explained in  
 19 the pages following, using the position of Regional Line Maintainer – Regular Staff and  
 20 the 2009 cost composition, as an example.

1 2.1.1. Payroll Obligations (\$57.83)

2  
3 A brief description of the cost elements included in this category is provided below.  
4 Compensation, wages and benefits are more fully explained in Exhibit C1, Tab 3,  
5 Schedule 2.

6  
7 Base Labour and Payroll Allowances (65% of Payroll Obligations)

- 8  
9
  - Base Pay: Contractually negotiated and reflected in wage schedules.
  - Payroll Allowances: Allowances are also contractually negotiated and stated in  
10 collective agreements. Regular staff (PWU) are entitled to travel, footwear and on-  
11 call allowances. Casual trades are entitled to board and travel allowances where  
12 circumstances require it.

13  
14  
15 Company Benefits (31% of Payroll Obligations)

- 16  
17
  - Regular Staff: Comprising pension (26.8% of base pensionable earnings) and current  
18 and post employment benefits; health, dental, etc. (30% of base pensionable  
19 earnings).
  - Non-Regular Staff (for example, casual trades): Pension and welfare contributions  
20 made on behalf of the regular employee. These contributions are significantly lower  
21 in comparison to the Company benefit contributions made on behalf of the regular  
22 employee.

23  
24  
25 Government Obligations (4% of Payroll Obligations)

- 26  
27
  - Consists of Canada Pension Plan (CPP), Employment Insurance (EI), Employee  
28 Health Tax (EHT) and Workplace Safety and Insurance Board (WSIB) contributions.

1    2.1.2. Contractual Time Away from Work (\$14.29)

2  
3    This category consists primarily of employee vacation and statutory holidays, all  
4    established and identified in the Company's collective agreements. Sickness and  
5    accident costs are also included and are based on historical trends and consider current  
6    Company initiatives.

7  
8    2.1.3. Time Not Directly Benefiting a Specific Program or Project (\$10.37)

9  
10   This category includes time for attendance of safety meetings, housekeeping and  
11   downtime often created due to inclement weather. These estimates are based primarily  
12   on historical trends.

13  
14   2.1.4 Field Supervision and Technical Support (\$13.04)

15  
16   This category includes the costs associated with field trades supervision and other  
17   management and technical staff providing support services to manage and monitor the  
18   status of the assigned programs and projects.

19  
20   2.1.5. Support Activities (\$13.47)

21  
22   Administrative Expenses and Centralized Support (72% of Support Activities)

- 23  
24   • These costs include administrative expenses such as travel costs, cell-phones and  
25   other miscellaneous expenses that cannot be specifically attributed to a particular  
26   program or project. Also included is an assignment of costs for centralized clerical  
27   support activities and other centralized support to maintain mobile radios and  
28   facilitate work management system requirements.

1 Work Methods & Training (16% of Support Activities)

- 2
- 3 • Costs to design, develop and deliver work methods and training programs. Costs are  
4 assigned based on the forecast consumption of these services as agreed to by the  
5 Work Methods & Training function and service recipient.
- 6

7 Safety & Environmental Support (12% of Support Activities)

- 8
- 9 • Costs to design, develop and deliver safety and environmental practices primarily for  
10 staff working in field locations. Costs are assigned based on the forecast  
11 consumption of these services as agreed to by the Safety & Environment function and  
12 the service recipient.
- 13

14 **2.2 Fleet Rate**

15

16 Hydro One controls and manages about 5,881 vehicles and other fleet equipment to  
17 support its work programs used for both Distribution and Transmission work. Fleet  
18 Management is described in Section 3.0 of this Exhibit.

19

20 Fleet assets are categorized into 65 classes of equipment. For each equipment class, a  
21 standard equipment rate is calculated by dividing the annual forecast cost to maintain  
22 each class of equipment by the annual forecast hours that the class of equipment is  
23 required to work (utilization hours). Utilization hours are derived based on a review of  
24 historical trends and an annual review of the upcoming work program. Utilization hours  
25 are defined as the hours the equipment is being used “on the job”. Table 2, below, shows  
26 the hourly fleet rate for the class of vehicle most commonly used by the Distribution  
27 business (a line maintenance truck) for historical, bridge and test years, illustrating that  
28 the rate includes all costs attributable to the benefiting work.

29

**Table 2**  
**Fleet Rate - Line Maintenance Truck**

	Historic			Bridge	Test	Test
	2006	2007	2008	2009	2010	2011
Operations & Repairs	30.00	34.00	37.00	25.00	34.00	36.00
Fuel Costs	5.00	6.00	6.00	7.00	8.00	8.00
Depreciation	25.00	20.00	20.00	18.00	18.00	19.00
<b>Hourly Rate</b>	<b>60.00</b>	<b>60.00</b>	<b>63.00</b>	<b>50.00</b>	<b>60.00</b>	<b>63.00</b>

Although the hourly amount for each variable comprising the fleet rate will fluctuate over time, the overall rate for a line maintenance truck is expected to remain relatively stable in future years. For example, fuel costs have increased and further increases are expected. Operations and Repairs costs in test years 2010 and 2011 are expected to increase by 36% and 43% respectively over bridge year 2009. Two of the reasons for the increases are:

- the maintenance required for the potentially surplus units;
- the dissipation of the savings achieved in 2009 from lower repairs and inspections of equipment purchased in the last 3 years.

Depreciation costs will increase by an average of 3% in test years 2010 and 2011 over bridge year 2009.

Below is a brief description of each category, with percentages reflective of the 2009 fleet rate.

**Operations & Repair Costs (50% of Fleet Rate)**

- This cost category consists primarily of repair costs (labour and parts) which are derived based on a forecast of the annual maintenance schedules for each piece of equipment. The age and the history of the vehicles are considered in the calculation. Throughout the year, all repair costs are charged directly to each piece of equipment.

1 Operations cost include administration staff and their allocated share of central  
2 service support costs (for example, work methods and safety training activities).

3

4 Fuel Cost (14% of Fleet Rate)

5

6 • Fuel consumption cost is calculated based on past history (including distance driven),  
7 future fuel price projections and the composition of the class.

8

9 Depreciation (36% of Fleet Rate)

10

11 • The depreciation for each class is calculated based on Hydro One's current  
12 depreciation policies, the current composition of other fleet and the annual forecast  
13 additions and deletions.

14

15 External Fleet Rentals

16

17 Due to the seasonal and fluctuating nature of the work program, Hydro One Distribution  
18 requires externally owned equipment to meet work program peaks. Similar to the process  
19 used to cost its own fleet, Hydro One Distribution calculates and uses standard rates to  
20 distribute these costs to programs and projects.

21

## 22 **2.3 Material Surcharge Rate**

23

24 A standard material surcharge rate, which captures supply chain procurement costs  
25 benefiting a particular program or project, is applied to material costs. (A detailed  
26 description of Hydro One's approach to supply chain management is found in Section 4.0  
27 of this Exhibit.)

28

1 Material costs charged to a project or program is based on the issue cost from Inventory,  
2 which is the Average Unit Price (AUP) or the direct-shipped purchase order price. On a  
3 monthly basis, total monthly material charges are surcharged with a fixed percentage cost  
4 to recover costs associated with purchasing, transportation and inventory management.  
5 The percentages range from 5% to 15%, depending on work program service  
6 requirements. The percentages are derived by assigning the costs of these activities to the  
7 work programs based on an annual assessment of the consumption of these services  
8 divided by the annual forecast of purchased material.

9  
10 The costs recovered in the surcharge are as follows:

- 11 • Hydro One Costs: Management, demand planning, warehousing and transportation  
12 of material (comprising approximately 60% of the total costs).
- 13 • Inergi Contract Costs: Procurement and investment recovery (comprising  
14 approximately 40% of the total costs).

#### 15 16 **2.4 Other Program and Project Costs**

17  
18 Depending on the nature of the work, Hydro One Distribution's program or project costs  
19 also include additional costs beyond the major contributors identified above. These  
20 additional costs may include the costs of external contractors and/or miscellaneous job  
21 specific consumables such as travel expenses or the purchase of low value material.

22  
23 In terms of estimating and costing of capital work, there may be circumstances when  
24 removal costs or customer contributions need to be separately identified. In these cases,  
25 the cost of removal work is accounted for as depreciation, and customer contributions are  
26 netted against gross capital costs.

1 Capital work also receives a monthly charge for its share of corporate interest and  
2 overhead costs. The composition of these two cost categories and the annual calculation  
3 are explained in Exhibit D1, Tab 4, Schedule 1, Allowances for Funds Used During  
4 Construction and Exhibit C1, Tab 5, Schedule 2, Overhead Capitalization.

5

6 **2.5 Standard Rates**

7

8 When using standard rates, residual costs naturally arise when actual costs incurred differ  
9 from the standards. These variances are accounted for on a monthly basis and assigned to  
10 both capital and maintenance programs. The monthly assignments of residual costs are  
11 made to OM&A and Capital based on the program and project cost activities responsible  
12 for generating the year-to-date variances.

13

14 **3.0 FLEET MANAGEMENT SERVICES**

15

16 Fleet Management Services provides centralized and turnkey services that include  
17 maintenance, administration, vehicle replacement and disposal. Vehicles are maintained  
18 to an optimum level to ensure public and employee safety and compliance with laws and  
19 Ministry regulations, including, but not limited to, CSA225, the Highway Traffic Act and  
20 the Commercial Vehicle Operator's Registration regulations. Fleet Management Services  
21 also ensures that environmental impacts are minimized, and line-of-business productivity  
22 is optimized by minimizing downtime, and travel time, and by optimizing technology and  
23 continuous improvement opportunities.

24

1 Fleet Management Services has adapted to the changing needs of its business by:

- 2
- 3 • Revising the Company's model for responding to internal customers from fixed zone  
4 service to a mobile and fire hall model, with maintenance garages strategically placed  
5 throughout the Province to facilitate a more rapid turnaround for vehicle servicing;
  - 6 • Rationalizing the Company's fleet and facilities (that is, optimizing the number of  
7 garages and geographical locations served);
  - 8 • Reducing equipment downtime and improving our equipment utilization;
  - 9 • Providing more competitive and cost efficient fleet support;
  - 10 • Adopting a flexible service delivery model that matches the nomadic and variable  
11 work program needs of Hydro One's lines of business with service delivery options  
12 that mirror private sector practices. Such options include shift work, extended hours  
13 of service and mobile service delivery;
  - 14 • Developing more timely, strategic and cost-efficient processes for equipment  
15 procurement and disposal;
  - 16 • Developing a long-range capital replacement program; and
  - 17 • Adopting data collection and information management systems that match the  
18 nomadic requirements of the Company's business units.
- 19

### 20 **3.1 Maintenance Model**

21

22 Fleet Management Services has developed a balanced maintenance model for mobile  
23 service delivery and centralized facilities. This model provides for 37 provincial  
24 locations and balances geographical customer requirements, travel time, third party  
25 vendor support and response time. Mobile/satellite repair units minimize costs by  
26 providing timely on-site field support for various nomadic work programs, such as  
27 vegetation control, new construction and off-road tower maintenance. Services provided  
28 to the lines of business and to any external parties (such as OPG) meet the rigorous

1 requirements of Fleet Management Services' agreements and are structured as a mobile  
2 and fire hall operating model to meet customer requirements.

### 3 4 **3.2 Managed Systems**

5  
6 The strategic alliance to implement a fleet management system ("FMS"), developed with  
7 Automotive Resources International ("ARI") in 2003, was renewed in 2008. The  
8 implementation of the FMS created an automated web-based system that uses a single  
9 credit card for each vehicle to capture all operating costs including fuel, parts and repairs.  
10 The FMS also incorporates programs to manage contracts, such as tender agreements,  
11 and the system prescribes spending guidelines and negotiated discounts. The system  
12 measures a variety of targets that reconcile approved purchase orders, estimates versus  
13 actuals, and vendor-related expenditures, discounts and complaints.

14  
15 The benefits of the FMS include:

- 16
- 17 • Improved scheduling of preventative maintenance, reduced repair times, travel time  
18 and reduced equipment downtime;
  - 19 • Increased access to a number of vendors for fuel, repairs and parts, thus minimizing  
20 cost and downtime;
  - 21 • Improved cost and efficiency, through carefully-considered procurement strategies  
22 and economies of scale, including improved volume discounts for fuel, parts and  
23 service;
  - 24 • A 1-800 number for repairs, roadside assistance and towing and improved reporting  
25 and data collection.
- 26

27 The FMS uses a variety of linked programs to manage the data and information for all  
28 facets of the business, including internal and external repairs. This system and associated

1 programs are operated in partnership with ARI, and take advantage of internal and  
2 external intelligence and technology.

3  
4 The maintenance program minimizes avoidable and expensive repairs and minimizes  
5 equipment downtime, which results in improved equipment utilization. Both internal and  
6 external service providers have access to the appropriate information through state-of-  
7 the-art automated management systems, allowing for quality decision-making at all levels  
8 of the maintenance program. Examples of the information provided include:

- 9
- 10 • Real time vehicle history;
  - 11 • Warranty criteria and warranty recovery;
  - 12 • A work and resources scheduling tool;
  - 13 • A pending and overdue work information alert system;
  - 14 • Product information, including vendor-specific information;
  - 15 • Repair and safe practices manuals;
  - 16 • Process and policy information;
  - 17 • Invoice and cost-management details;
  - 18 • Monthly and ad-hoc reports; and
  - 19 • Work order management.
- 20

### 21 **3.3 Fleet Complement and Utilization**

22

23 Fleet Management Services controls and manages approximately 5,881 vehicles and  
24 other equipment primarily for distribution and transmission work. Inventory levels are  
25 controlled and set by the Hydro One Distribution lines of business and Fleet Management  
26 Services within the guidelines set for staffing versus fleet ratio, type and volume of work  
27 programs, geographic locations and utilization targets. The increase in the fleet  
28 complement, therefore, is directly related to the increase in the Company's work on

1 system infrastructure and corresponding staffing levels. Fleet Management Services  
2 maintains 37 facilities to support 19 forestry locations and two brushing crews, 1,005  
3 distribution stations, 279 transmission stations, 53 Provincial lines distribution locations  
4 and five transmission locations.

5  
6 As capital and OM&A investments have been increasing, the options to meet increased  
7 equipment demand include the purchase, lease or rental of additional equipment, or  
8 increased utilization of existing equipment. The optimum option is to increase  
9 utilization, which minimizes capital investment compared to the option of additional  
10 purchases. Simultaneously, it maximizes the advantage of owned core equipment versus  
11 the additional cost of external rentals, which is 30 percent higher than owned equipment  
12 rates. This assessment is based on an internal comparison of the actual costs of  
13 equipment rentals versus those of owned core equipment.

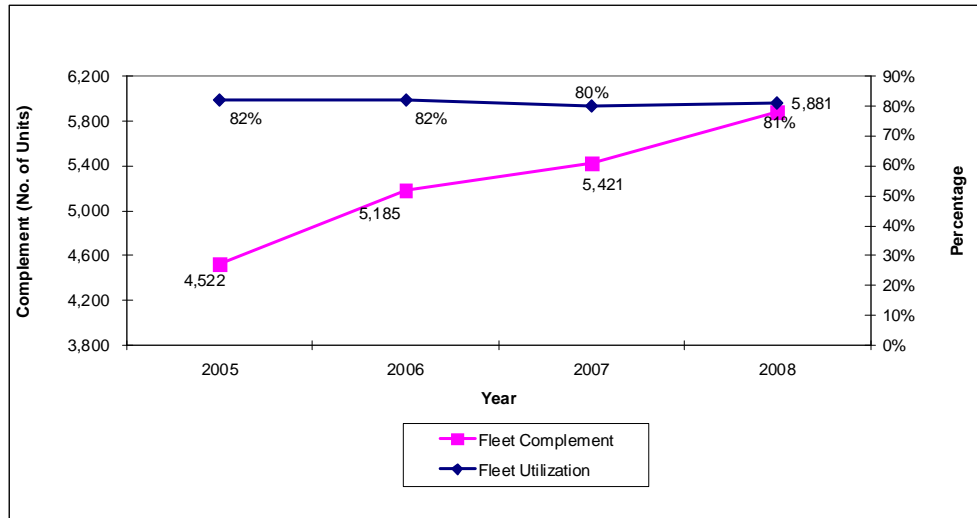
14  
15 The benefits of improving utilization include:

- 16
- 17 • decreased long term capital requirements;
  - 18 • improved ability to respond to fluctuations in work programs; and
  - 19 • reduced rental costs, with a correspondingly lower impact on the Company's OM&A  
20 budget.

21  
22 Equipment utilization averages have increased from approximately 65 percent in 2001 to  
23 approximately 81 percent in 2008. The 2008 average equipment rate is \$23.34; this is  
24 established by averaging all the individual equipment rates.

1  
2

**Figure 1 – Fleet Complement & Utilization**



3

4

### 3.4 Fleet Management Services Budget

5

6  
7 Fleet Management Services' annual budget is developed and managed based on the all-in  
8 costs of operating the fleet and the following criteria:

- 9 • Historical and forecast fixed and variable costs including fuel, depreciation,  
10 maintenance and repair, labour/staffing, external rentals and corporate allocations.
- 11 • Historical cost and mechanical fitness evaluations.
- 12 • Work program forecasts provided by the lines of business.
- 13 • Estimates provided by internal and external providers.
- 14 • The requirements of the capital/vehicle replacement program.
- 15 • Projected escalators.

16

17 Table 3, below, provides total expenditures on the components comprising the fleet rate  
18 for historic, bridge and test years.

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22

**Table 3**  
**Fleet Management Services Budget Expenditures**  
**(\$ Million)**

	Historic			Bridge	Test	Test
	2006	2007	2008	2009	2010	2011
Operations & Repairs	47.0	49.0	53.0	50.0	58.0	60.0
Depreciation	26.0	28.0	31.0	33.0	36.0	39.0
Fuel	19.0	20.0	24.0	22.0	28.0	29.0
<b>Subtotal</b>	<b>92.0</b>	<b>97.0</b>	<b>108.0</b>	<b>105.0</b>	<b>122.0</b>	<b>128.0</b>
Rentals	8.0	9.0	6.0	9.0	7.0	6.0
<b>Total</b>	<b>100.0</b>	<b>106.0</b>	<b>114.0</b>	<b>114.0</b>	<b>129.0</b>	<b>134.0</b>

3.4.1 Operations and Repairs

This cost category primarily consists of repair costs (external and internal labour and parts), the budget for which is based on a forecast of the annual maintenance schedules for each piece of equipment. The age and the history of the vehicles are considered in the calculations. Throughout the year, all repair costs are charged directly to each piece of equipment. Operations costs include wages, an allocated share of facility and telecommunication costs, and work methods and safety training activities.

3.4.2 Depreciation

The depreciation for each class within the fleet is calculated based on the current depreciation policies in Hydro One, and considers the current composition of the fleet, and annual forecast additions and deletions. Lease costs associated with Fleet’s operating leases are also included in this category. Fleet currently leases approximately one percent of its vehicles, predominately light trucks.

1    3.4.3   Fuel Cost

2  
3    Fuel cost per class of equipment is calculated based on past history and current market  
4    projections as well as the current composition of the class. Throughout the year, fuel  
5    costs are charged directly to the particular piece of equipment consuming the fuel.

6  
7    3.4.4   External Fleet Rentals

8  
9    Due to the seasonal and fluctuating nature of the Company's work program, Hydro One  
10    Distribution requires the use of externally-owned equipment to meet the peaks in its  
11    programs. Using a process similar to that used to cost Hydro One Distribution's own  
12    fleet, standard rates are calculated and costs are distributed to the Company's programs  
13    and projects.

14  
15    **4.0    SUPPLY CHAIN MANAGEMENT**

16  
17    Hydro One delivers end-to-end supply chain services for the Distribution, Transmission  
18    and Remotes businesses. The focus is on the right product with the right quality, at the  
19    right place, right time and at the right cost.

20  
21    The proposed 2010 costs for Supply Chain Services are expected to be \$35.7 million,  
22    with a slight decrease to \$35.2 million in 2011. These services include strategic sourcing  
23    (purchase) of materials and services, storage and distribution of materials; demand  
24    planning, inspection services, transportation, inventory management, and investment  
25    recovery of disposed assets.

26  
27    Supply Chain Services costs are allocated to work programs and projects through the  
28    material surcharge rate.

1 This section describes the budgeted cost levels, followed by a description of the  
2 components of Supply Chain Management.

3  
4 **Table 4**  
5 **Supply Chain**  
6 **(\$ Million)**  
7

	Historic			Bridge	Test	Test
	2006	2007	2008	2009	2010	2011
<b>Total</b>	23.5	28.0	29.3	34.6	35.7	35.2

8  
9 The increase in supply chain costs between 2006 to 2009 reflects the increase in  
10 transaction volumes, as well as cost increases related to transportation and warehousing,  
11 factory and manufacturing inspections, demand planning and expediting requirements.

12  
13 For the 2009 to 2011 period, supply chain management has experienced an average  
14 increase of 2%. This increase reflects the support for the growth in the capital and  
15 OM&A work programs across the organization.

16  
17 Hydro One Distribution's supply chain is a non-core service which has been out-sourced  
18 to Inergi L.P. The components of supply chain management performed by Inergi include  
19 sourcing (purchase) of materials and services, transportation, contract management and  
20 investment recovery.

21  
22 This agreement was contracted for the same service levels at a declining price over the  
23 term of the contract. The increasing overall cost levels represent enhanced service levels  
24 to meet business needs in the areas of contract management, inventory management,  
25 sourcing and demand planning.

1     **4.1     Supply Chain Policies and Procedures**

2  
3     Hydro One Distribution operates a fair and transparent procurement process that gives all  
4     companies equal opportunity to do business consistent with its Procurement Policy and  
5     Principles.

6  
7     Tenders and proposals are evaluated based on predefined evaluation criteria by cross-  
8     functional teams. The outcome of the evaluation is the foundation for awarding  
9     procurement contracts.

10  
11    **4.2     Sourcing of Materials and Services**

12  
13    The sourcing of materials and services, primarily carried out within Inergi, includes the  
14    following:

- 15
- 16       • Demand Management and Procurement – Market intelligence with respect to  
17       commodities, processing purchase transactions and inspecting and expediting  
18       services to ensure delivery to contract commitments.
  - 19       • Sourcing and Vendor Management – Services to support sourcing all  
20       commodities and services which include managing the size and composition of  
21       the vendor base, resolving issues, managing inventory levels and negotiating  
22       stocking arrangements.

23  
24    Hydro One Distribution manages its procurement and supply base by using strategic  
25    sourcing in the acquisition of goods and services. Strategic sourcing is a disciplined  
26    business process for purchasing goods and services on a Company-wide basis using  
27    cross-functional teams to manage the supply base as a valued resource. The

1 methodology's five-step process includes spending analysis, market analysis,  
2 development of a sourcing strategy, negotiation and award and contract management.

### 3 4 **4.3 Inspection Services**

5  
6 Inergi LP is engaged to provide timely inspection services to assure that products are  
7 manufactured in accordance to specifications established by Hydro One Distribution, and  
8 tracks costs and schedules on a product and project basis. For example, Hydro One has  
9 undertaken a replacement program for a wide range of its transformers that are near their  
10 end-of-life.

### 11 12 **4.4 Storage and Distribution of Materials - Warehousing**

13  
14 Hydro One Distribution's central warehouse operation in Barrie is responsible for the  
15 storage and distribution of materials for the service centres and station locations. This  
16 warehouse services two primary customers, Customer Operations and Grid Operations.  
17 Ten stock-keepers are assigned to the central warehouse. Customer Operations utilizes 18  
18 field stock-keepers to service 64 field service centres. Similarly, Grid Operations  
19 leverages 31 Planning and Scheduling Technicians (PST's) at 22 stations. The field  
20 stock-keepers and PST's are responsible for receiving shipments and for storing and  
21 ordering material. Deliveries to the service centres are contracted to a third party  
22 transportation carrier.

23  
24 The intent of a consolidated warehouse operation is to realize efficiencies through  
25 focusing on activities such as:

- 26  
27
- Improving business processes such as receipting, shipping and cycle counting;

- 1       • Streamlining direct shipping, minimizing cross-docking and continuous  
2       evaluation of material required for inventory;
- 3       • Exploring the options of technology such as bar coding to improve operating  
4       efficiencies such as receipting, cycle counting, shipping and tracking inventory;
- 5       • Managing and coordinating the delivery of materials on the scheduled delivery  
6       date to the service centres to ensure that the field operation receives the right  
7       material at the right time;
- 8       • Improving receipting efficiency by integrating with the contracted transportation  
9       company to provide visibility into the supply chain and scheduling the inbound  
10      shipment.

11

#### 12   **4.5    Transportation**

13

14   Hydro One Distribution manages its inbound and outbound transportation of materials  
15   through contracts with third party companies. In 2007, Hydro One Distribution entered  
16   into such a contract for material flowing in and out of the central warehouse. The  
17   strategy is to actively manage the cost of such traffic and reduce transportation cost year  
18   over year.

19

#### 20   **4.6    Investment Recovery**

21

22   The final step of the supply chain is the disposal and investment recovery of end-of-life  
23   assets. This recovery is typically in the range of \$3.9 million to \$6.7 million per year,  
24   and primarily involves vehicle sales and scrap metal. Hydro One Distribution continues  
25   to focus on extracting the maximum value possible from the sale of these assets.

26

27   A breakdown of the sale of assets is as follows:

28

**Table 5**  
**Breakdown of Sales of Assets through Investment Recovery Program**  
**(\$ Million)**

Type of Sale	Recovery 2006	Recovery 2007	Recovery 2008
Vehicle Sales	1.82	0.80	1.09
Scrap Metal	2.03	4.20	5.53
Tools	0.05	0.06	0.07
<b>Total</b>	<b>3.91</b>	<b>5.06</b>	<b>6.69</b>

#### **4.7 Cost Savings from Strategic Sourcing**

Since 2005, due to its strategic sourcing imitative, Hydro One Networks has realized \$26 million in cumulative savings in the purchase of major equipment, commodities and services such as power transformers, circuit breakers, wood poles, distribution transformers, wire and cable, and pole and line hardware. Strategic sourcing results vary from commodity to commodity or from one service to another.

The main benefits of sourcing strategies are described below:

- Active involvement of internal stakeholders to communicate their business needs for the products and services;
- Cost reduction by increased leverage of Company-wide expenditures – purchases are consolidated by commodity and/or service to ensure that the business receives maximum value. This eliminates the need to tender and purchase as requirements surface -- an added benefit of this approach;
- Reduced total life cycle cost for materials and services – when purchasing equipment, all aspects are identified to ensure that Hydro One Distribution acquires maximum value for the life cycle of the equipment. For example, specifications, maintenance requirements, installation services and warranty services are defined and reviewed to ensure that business needs will be met, and

1 order and invoice processes, lead time and inventory requirements, etc. are  
2 evaluated to determine where greater efficiencies may be realized;

- 3 • Improved security of supply through longer-term agreements. To maximize  
4 value, longer-term agreements are established with fixed prices, or formula  
5 pricing is considered to ensure that Hydro One Distribution achieves best value;
- 6 • Improved and/or consistent quality of material and services.

7

8 Strategic sourcing will continue to be a major focus, as the Company emphasizes cost  
9 control and security of supply during a volatile commodity market, while demand in the  
10 global utility sector increases.

11

#### 12 **4.8 Recent Productivity Improvements in Supply Chain Management**

13

14 Hydro One Distribution is interested in continuous improvement, and supply chain  
15 management is one example. This section details some work in progress to provide  
16 effectiveness and efficiency gains.

17

18 Previously, procurement of material for projects usually occurred after the release of the  
19 project. The supply management process is evolving, however, to consider the broader  
20 work program over multiple years, and obtain quotes for materials required over multiple  
21 delivery dates. This approach assists vendors by allowing them to better plan their  
22 activities, and leads to lower costs and a stronger relationship between Hydro One  
23 Distribution and the vendor – which has additional benefits if difficulties arise in the  
24 supply of materials.

25

26 Hydro One Distribution has also developed “blanket purchasing orders” with vendors to  
27 establish a standing order or relationship for critical materials, such as cable and

1 autotransformers. In addition, the Company involves some suppliers in its planning  
2 activities, and studies historical buying patterns to assist in planning purchases.

3

4 Streamlining standards is another way in which Hydro One Distribution is improving the  
5 strategic sourcing process. For large power transformers, for example, the Company  
6 currently has approximately 150 standards, which are being reduced to about 15. In  
7 addition to simplifying procurement, this also increases both the likelihood that spares  
8 will be available for use, and the ease of maintaining a lower inventory.