



# **Standing Committee on Crown Corporations**

## **Hansard Verbatim Report**

**No. 47 – June 9, 1998**



**Legislative Assembly of Saskatchewan**

**Twenty-third Legislature**

**STANDING COMMITTEE ON CROWN CORPORATIONS  
1998**

Pat Lorje, Chair  
Saskatoon Southeast

Kim Trew, Vice-Chair  
Regina Coronation Park

Bob Bjornerud  
Saltcoats

Doreen Hamilton  
Regina Wascana Plains

Ben Heppner  
Rosthern

Jack Hillson  
North Battleford

Lloyd Johnson  
Shellbrook-Spiritwood

Lindy Kasperski  
Regina Sherwood

Myron Kowalsky  
Prince Albert Carlton

Andy Renaud  
Carrot River Valley

**Channel Lake Petroleum Ltd.**

**The Chair:** — Good morning everyone. We will now reconvene the special Crown Corporations Committee hearings into the Channel Lake circumstances.

We have today . . . we will be hearing testimony from representatives of Ernst & Young, the auditors of record for SaskPower. Before I begin the customary statement to witnesses and swearing in of the witnesses, I should inform . . . could I have the committee members' attention, please, just for a few minutes.

Before I swear in the witnesses, I would like to inform committee members that we do have a request from the two auditors — one from Regina and the other currently resident in Calgary, but originally from Swift Current — that they would like to testify simultaneously because they worked on the report simultaneously. It's a similar request to the one we had from Deloitte Touche.

How do committee members feel about it, understanding of course that this will not create a precedent. We will be handling these kinds of requests on an individual case-by-case basis. Do I have agreement from the committee that I'll swear them both in simultaneously? Thank you for that. If you could just wait a moment then, we seem to have lost the Bible. Excuse me, I have been informed that you can swear without a Bible but luckily we just found it.

Committee members we have before us today Rupert James from Ernst & Young in Regina. Committee members will be very familiar with Rupert because he does come to this committee fairly often and he also has a very high profile in the Regina community as an excellent volunteer.

Committee members, I would also like to introduce you to Barry Munro from Calgary. As I indicated, he's originally a Saskatchewan boy and this is his first time in the Legislative Building. And he will be looking forward to taking a tour afterwards, something he missed many, many years ago.

Gentlemen, before I swear you in I have a statement that I have to read to you. It is a customary statement that's read to all witnesses.

Witnesses should be aware that when appearing before a legislative committee your testimony is entitled to have the protection of parliamentary privilege. The evidence you provide to this committee cannot be used against you as the subject of a civil action.

In addition, I wish to advise you that you are protected by section 13 of the Canadian Charter of Rights and Freedoms which provides that:

A witness who testifies in any proceedings has the right not to have any incriminating evidence so given used to incriminate that witness in any other proceedings, except in a prosecution for perjury or for the giving of contradictory evidence.

A witness must answer all questions put by the committee. You are advised that you may be recalled to appear again before this committee at a later date if the committee so decides. You are reminded to please address all comments through the Chair. Thank you.

I would also say, in addition, that the committee has decided that all witnesses will be accorded the privilege of making an opening statement to the committee and if they so wish, a closing statement. The closing statement may either be oral at the end of your testimony today or it may be in written form.

I'll now swear you in. Rupert, did you wish to swear or affirm?

**Mr. James:** — Swear.

**The Chair:** — Do you swear that the evidence you shall give on this examination shall be the truth, the whole truth, and nothing but the truth, so help you God.

**Mr. James:** — I do.

**The Chair:** — Thank you.

Barry . . .

**Mr. Munro:** — Swear.

**The Chair:** — Do you swear that the evidence you shall give on this examination shall be the truth, the whole truth, and nothing but the truth, so help you God?

**Mr. Munro:** — I do.

**The Chair:** — Gentlemen, do you have an opening statement?

**Mr. James:** — Yes we do, Madam Chair. And I have 20 copies of it beside me here.

**The Chair:** — Mr. James, go ahead.

**Mr. James:** — Thank you, Madam Chair. And I would like to thank the committee before reading the opening comments for your agreeing to have us sit together at this table. When we perform audit work and involve other professionals within our firm, it is customary to work together. And I hope that this will facilitate the process of answering your questions.

And at the end of the remarks I'll try to give you a little guidance as to who you might want to try to direct the questions to in terms of our respective roles. But I think that will become clear in the opening remarks.

Good morning, Madam Chair, and members of the Standing Committee on Crown Corporations. My name is Rupert James. I am a chartered accountant and a partner of Ernst & Young in Regina. Ernst & Young is a national firm of chartered accountants and management consultants with offices in Regina and Saskatoon and major cities across Canada.

I would like to take this opportunity to explain our role as auditors of Saskatchewan Power Corporation, herein referred to

as SaskPower, and Channel Lake Petroleum Ltd., herein referred to as Channel Lake.

Mr. Barry Munro, a partner from our Calgary office, is with me today. Mr. Munro began his professional career with Ernst & Young in Saskatchewan. He is also a chartered accountant and a member of the Institute of Chartered Accountants of Saskatchewan and Alberta.

We hope that our appearance today and our responses to your queries will bring additional insight to you with respect to our professional engagements with both SaskPower and Channel Lake.

To prepare for today's testimony, we reviewed our audit working paper files for the years 1993 through 1997. Mr. Munro and I discussed key events that we could recall throughout this period. We were interviewed by Deloitte & Touche as part of their preparation of their report to Crown Investments Corporation. We have read their report together with the Crown Investments Corporation report regarding Channel Lake. We have followed to the best of our ability the committee testimony to date.

I shall read an opening statement that contains facts related to various aspects of our work, some of which pertain to my role and some of which pertain to Mr. Munro's role. Mr. Munro will not have a separate opening statement. We are both pleased to answer your questions following these opening remarks.

Our opening remarks are organized under eight headings: (1) the nature of our professional engagements with respect to SaskPower and Channel Lake; (2) our reporting relationship with the Provincial Auditor; (3) the role of Ernst & Young partners in these engagements, including Mr. Munro and myself; (4) the nature of our communications on Channel Lake matters; (5) events surrounding our audit of the 1996 Channel Lake financial statements; (6) our involvement with the sale of Channel Lake in 1997; (7) our engagement with Channel Lake subsequent to the sale of the company by SaskPower; and (8) our audit of the 1997 financial statements of SaskPower which reflected the accounting for the sale of Channel Lake and the Direct Energy Marketing Limited, herein referred to as Direct Energy, gas supply agreement.

Item (1): Nature of Ernst & Young's professional engagements. Our engagements relevant to the matters at hand included the audit of the financial statements of Channel Lake and the audit of the consolidated financial statements of SaskPower. The consolidated financial statements of SaskPower included, along with its other wholly owned entities, the financial results of Channel Lake for the period of time that Channel Lake was active and owned by SaskPower, that being part of 1993, all of 1994, 1995, and 1996, and part of 1997.

The professional standards of the Canadian Institute of Chartered Accountants require that we plan and perform an audit to obtain reasonable assurance that the financial statements prepared by management are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by

management, as well as evaluating the overall financial statement presentation. Our opinion on the financial statements appears in the auditor's report attached to the audited financial statements.

Under generally accepted auditing standards, in order to express an opinion on the fairness of presentation of the financial statements in accordance with generally accepted accounting principles, an auditor is not required to place reliance on a company's system of internal control. However, we chose to do so because our audits of SaskPower and Channel Lake were both in the Crown sector where we must report on the system of internal control. Accordingly we completed sufficient and appropriate audit procedures to place reliance on those systems.

During an audit, sometimes matters come to our attention related to business matters, internal controls, or areas of possible efficiency improvement that we wish to bring to management's attention. If in our judgement such an issue needs to be documented in written form with our client, we will issue what is often referred to as a management letter. A copy of the management letter is forwarded to the company's audit committee for their information and discussed with them at their request.

A management letter is not necessarily issued annually. Often we communicate verbally with our clients to provide suggestions on matters where we believe that management is able to take quick action or where our comments are already understood and accepted.

Item (2): Our reporting relationship with the Provincial Auditor. For Crown corporation audits, in addition to the auditor's report on the financial statements, we are required to issue three other auditors' reports addressed to the Provincial Auditor. These are: a report on the system of internal controls of the entity; a report on the entity's compliance with certain legislation; and a report on any other matters that come to our attention during the course of our audit of the annual financial statements.

Our planned audit procedures are reviewed by a representative of the Provincial Auditor in accordance with the recommendation of the task force on roles, responsibilities, and duties of auditors. We advise a representative of the Provincial Auditor, of significant matters that arise during the course of the audit while the audit is under way.

The representative of the Provincial Auditor also reviews our audit working papers and meets with us at the conclusion of the audit to discuss our findings, address any questions that he or she might have, and to share with us his or her own conclusions. The Provincial Auditor and/or his representatives often attend key meetings that we have with management and the audit and finance committee.

Item (3): Role of Mr. Rupert James, Regina office, and Mr. Barry Munro, Calgary office. We were engaged to perform an audit of Channel Lake in 1993, the period of time during which Channel Lake was first active. In that year I was the partner with direct responsibility for the audits of both SaskPower and Channel Lake. I was assisted by Mr. Munro of our Calgary office. Mr. Munro has significant professional experience in the oil and gas industry, and as is customary, we utilize such

expertise in the conduct of our work when warranted.

In subsequent years, Mr. Munro assumed more direct responsibility for the Channel Lake field work because many of the accounting records related to the day-to-day oil and gas production operations of Channel Lake were located in Calgary. Each year, Mr. Munro and I discussed our planned approach to the Channel Lake audit, including the reporting relationships with the two companies and SaskPower's requirements for preparing its consolidated financial statements and our audit thereof.

Mr. Munro's contacts and those of his staff in his audit of Channel Lake were primarily with the management of Channel Lake. The senior individuals with whom he had primary contact included Mr. Lawrence Portigal, as well as Mr. Phil Symchych and Ms. Liza Herdzig, contract accountants who worked on Channel Lake matters. Mr. Munro and his staff also had contact with the staff of the management company in Calgary, Management Ventures Inc., who operated the Channel Lake oil and gas properties. Mr. Munro also had some contact with SaskPower's controller, Ms. Pat Hall.

My contacts were primarily with the management of SaskPower, not only because of the fact that my staff and I were auditing the SaskPower legal entity, but because we were also auditing the consolidation of SaskPower with its subsidiaries. The senior individuals with whom I had contact on Channel Lake matters were Mr. Ken Christensen, Ms. Hall, and Mr. Rob Spelliscy. My staff and I had some contact with Mr. Portigal and Mr. Symchych from time to time.

I was Ernst & Young's primary contact with the audit and finance committee of SaskPower's board of directors.

Item (4): Nature of communications on Channel Lake matters. For the years 1993 through 1997 we issued our auditors' reports on the consolidated financial statements of SaskPower and our reports can be found in SaskPower's annual reports for those years. The 1993 to 1996 annual reports are your document numbers CLP 11/1 through CLP 11/4. We are not aware of the document reference for the 1997 annual report.

For the years 1993 through 1996, SaskPower's last full year or ownership of Channel Lake, we issued our auditors' reports on the financial statements of Channel Lake. These are your document numbers CLP 10/1 through CLP 10/4.

For the years 1993 through 1996 we issued our auditors' reports on the system of internal controls, legislative compliance, and other matters that came to our attention for both SaskPower and Channel Lake, to the Provincial Auditor. Your document numbers CLP 12/34 through CLP 12/35 are those reports for 1995 and 1996 relating to Channel Lake.

For 1993 and 1994 we also issued management letters to SaskPower's management and audit and finance committee dealing with various matters, some of which related to Channel Lake. The 1993 management letter is in CLP 7/1 as attached schedule A20/94. The 1994 management letter is CLP 7/6 as attached schedule A30/95.

In 1995 we did not issue a management letter to SaskPower's

management and audit and finance committee as there were no new matters to report.

In 1996 we did not issue a management letter because we had nothing to add in addition to our detailed auditor's report to the Provincial Auditor on internal control matters.

For clarification, we offer the following comments on the content of our various letters and reports.

Because the Channel Lake operations were new to SaskPower in 1993, a number of matters had yet to be clarified with respect to how the operations were going to be managed on an ongoing basis, including the responsibility within the company for the accounting records. Our 1993 management letter included recommendations to put in place a formal organizational reporting structure for Channel Lake to ensure timely and accurate accounting and financial reporting.

We recommended that accounting and reporting policies and procedures be clarified between SaskPower's finance group and the fuel supply task force. We also recommended that professional staff be hired, including a controller, with appropriate gas industry experience, who would be responsible for supervising the work of the Calgary based management company which was managing the day-to-day operations of Channel Lake. Management responded that they were in the process of finalizing the formal reporting structure and reviewing staffing options.

Our 1994 management letter to SaskPower contained five points related to Channel Lake. Three of these related to accounting processes and one related to matters to be addressed in the contractual arrangements with the Calgary based management company. We also made the observation that Channel Lake had been given the authority to engage in gas trading activities. In our management letter we pointed out that:

An active gas trading program represents a sensitive and significant activity for Channel Lake to engage in. We recommend that formal policies and procedures be developed, documented and approved by Channel Lake's Board of Directors to govern such gas trading activities.

When we issued our 1994 management letter in the spring of 1995, management was in the process of drafting gas trading policies and procedures. We reviewed two drafts of these policies and made comments on these at various times in 1995.

As part of our 1995 audits of both Channel Lake and SaskPower, we followed up on all points that were raised in our previous management letters. We were satisfied, based on our audit procedures and discussions with management of both companies, that all matters had either been addressed or were in the process of being addressed.

On that basis, and given the fact that there had been no changes in any of the personnel we were communicating with in SaskPower's and Channel Lake's management and on the SaskPower audit and finance committee between our 1994 and 1995 audits, we did not issue a separate management letter for 1995.

At the conclusion of our 1995 audit of Channel Lake, we met with Mr. Portigal and discussed all 1994 management letter points including the progress being made to develop and formalize Channel Lake's gas trading policies. We also met with SaskPower's audit and finance committee, and we advised the audit and finance committee that the matters we had brought to their attention through our 1994 management letter had either been addressed or were in the process of being addressed. In particular, we reported to the committee that gas trading policies and procedures still needed to be finalized.

For 1996 we issued our auditor's report on internal controls to the Provincial Auditor. This is your document CLP 12/35. Our opinion was qualified for a number of items. In our report we stated that in 1996 Channel Lake became an active gas trader, having entered into 104 gas arbitrage deals.

We reported on the lack of approved policies. These were still in draft form and it was difficult to determine if they had been used. We reported that Channel Lake's credit approval process for most of 1996 was not as rigorous as it could have been. We reported, among other things, that the company's business plan outlining its gas trading business objectives should have been more specific with respect to the business risks involved in gas trading, and that the company's reporting process relating to its gas trading activities could have been more comprehensive.

All of the above mentioned matters were reported to the Provincial Auditor during the course of our work. The Provincial Auditor in turn issued his reports to the legislature, which contained these items.

Item (5): Events surrounding our audit of the 1996 Channel Lake financial statements and the issuance of those financial statements.

In October 1996 we began the planning process for our audit of the 1996 financial statements of Channel Lake. Our audit procedures were designed: (a) for purposes of reporting on the consolidated financial statements of SaskPower for the year ended December 31, 1996; and (b) to allow us to issue a separate audit opinion on the financial statements of Channel Lake for the year ended December 31, 1996.

We completed our tests of internal controls and our pre-year-end audit work in November of 1996. Procedures with respect to Channel Lake's oil and gas operations were carried out in Channel Lake's Calgary office, and procedures with respect to Channel Lake's gas trading operations were carried out in Channel Lake's Regina office. Both the Calgary and the Regina work was staffed by Ernst & Young in Calgary in order to ensure that we dedicated sufficient oil and gas expertise to the audit.

While we were at Channel Lake's Regina office in November 1996, we were informed by management that two of Channel Lake's gas trading counterparties, Multi Energies Inc. and NESI Energy Marketing Canada Ltd. had declared bankruptcy. We determined that Channel Lake would be exposed on open positions from its arbitrage gas trading contracts with those parties.

Our original planned audit procedures were designed to gain an

understanding of Channel Lake's gas trading activities and the controls surrounding those activities, and then to test the controls and actual completed transactions as we deemed appropriate.

As a result of the two bankruptcies, we extended our original procedures to include the initial calculation of the extent of contingent exposure that Channel Lake had with respect to gas trading losses. We prepared detailed documentation for our files during November and December 1996 on these matters and discussed the potential gas trading losses with Channel Lake management, SaskPower's finance group management, and staff of the Provincial Auditor as part of their review of our 1996 audit planning files.

We substantially completed our audit of the 1996 financial statements of Channel Lake on January 31, 1997, and draft financial statements were prepared by Channel Lake management and reviewed by us at that time. Those financial statements form a part of the consolidated financial statements of SaskPower for the year ended December 31, 1996 on which we issued our auditor's report dated February 3, 1997.

The Channel Lake 1996 financial statements reflected aggregate losses of approximately \$400,000 resulting from the write-off of accounts receivable due from the bankrupt Multi Energies Inc. and gas trading losses of approximately \$2.4 million relating to the closing out of open gas trading positions to December 31, 1996. The draft financial statements also included a note (refer to note 11, Commitments and Contingencies) which sets out an estimate of the contingent losses to which Channel Lake was exposed resulting from the open gas trading contract positions.

Except for the final determination of the amount of contingent gas trading losses to which Channel Lake was exposed, which was dependent upon the calculation of the potential losses at a date close to when the financial statements were to be issued, the financial statements were in final form and ready to be submitted for approval by SaskPower prior to issuance.

On March 13, 1997 we met with Mr. Portigal to discuss outstanding matters related to the 1996 audit of Channel Lake. At that time, the only matters remaining to be resolved were making a final determination of the amount of gas trading losses to be disclosed in the notes to the financial statements and the completion of our reports on legislative compliance and internal controls to the Provincial Auditor. At that meeting, Mr. Portigal indicated that he was in the process of attempting to sell Channel Lake for SaskPower, with an attempt being made to complete a sale by March 31, 1997.

In April 1997 we became aware that Channel Lake had been sold to Direct Energy. We contacted Ms. Hall, SaskPower's controller, to ask her for an update on both the process of the sale of Channel Lake and the completion of the Channel Lake 1996 financial statements. We also requested that Ms. Hall provide us with a copy of the Channel Lake/Direct Energy purchase and sale agreement. Ms. Hall informed us that she had not been involved with the sale transaction. She did, however, arrange for the document to be sent to us by a Channel Lake staff member in Regina. We received a copy on May 5, 1997.

The agreement we received from Channel Lake was dated April 2, 1997 and was signed by both Direct Energy and SaskPower officials. We used this agreement to draft a subsequent event note to the Channel Lake financial statements and provided that note to both Mr. Portigal at Channel Lake and Ms. Hall at SaskPower for their review and approval. (Refer to note 12 to the Channel Lake 1996 audited financial statements).

On May 29, 1997 Mr. Portigal contacted us and asked that we issue our report on the final 1996 Channel Lake financial statements. Mr. Portigal had indicated to us that the final signed 1996 Channel Lake financial statements were required for the closing of the Channel Lake sale to Direct Energy.

We confirmed with Mr. Portigal that Channel Lake management was satisfied with the disclosures in those financial statements, and also confirmed with Mr. Hall at SaskPower that SaskPower management were satisfied with the form and presentation of the Channel Lake 1996 financial statements.

The final December 31, 1996 audited financial statements for Channel Lake were issued on May 30, 1997. Our auditor's report on these financial statements was split dated as follows, quote, "January 31, 1997 except for Notes 11 and 12 which are as of April 2, 1997". April 2, 1997 was selected as the second date because it coincided with the agreement date and represented the date to which we performed our work on the two notes referred to.

Note 11, entitled "Commitments and Contingencies", to those financial statements discloses that the company had aggregate estimated future gas trading losses at December 31, 1996 of approximately \$5.6 million. The calculation of this amount was based on gas prices as at March 31, 1997. Of this aggregate estimated amount, \$3.1 million in losses were realized in the three months ended March 31, 1997.

Note 12, entitled "Subsequent Events", to those financial statements discloses the agreement for sale of Channel Lake to Direct Energy. The subsequent event note discloses a sale price of \$20.8 million, which was extracted from clause 2.2 of the April 2, 1997 purchase and sale agreement.

In receiving approval for the final issuance of the financial statements, we were not informed, either by Channel Lake or SaskPower management that there was a concern about the mechanics of the adjustment clauses contained in the purchase and sale agreement or about any changes to the purchase price.

We did not receive any of the various internal memoranda from Mr. Portigal to SaskPower management, which we are now aware had been prepared as part of the Channel Lake sale process.

In addition, we were not informed by SaskPower's management that Mr. Portigal's contract had been terminated. We were informed by Mr. Portigal in June 1997 that he was going to continue to manage the Channel Lake operations on behalf of Direct Energy.

Our 1996 audit working papers and the draft Channel Lake financial statements were reviewed by staff of the Provincial

Auditor as part of their normal review procedures.

As noted earlier, as part of our engagement, we also issued a report on legislative compliance and a report on internal controls to the Provincial Auditor with respect to Channel Lake. First drafts of those reports were prepared in April, 1997 at which time we sought guidance from the Provincial Auditor as to how to disclose the internal control matters with respect to Channel Lake's gas trading activities. A draft of our reports was provided to Mr. Portigal for his review on May 9, 1997. We believe this is document CLP 17/2. He had no substantive comments on the presentation therein.

The draft reports were also presented at that time to SaskPower management. Staff of the Provincial Auditor also reviewed the May 9, 1997 draft version of our report in June, 1997. We received management comments in late June, 1997, and again in September 1997. Our final reports were issued to the Provincial Auditor in September 1997. These are the documents at CLP 12/35. Those reports were then used by the Provincial Auditor in the preparation of his 1997 fall report, volume 2.

Item (6): our involvement with the sale of Channel Lake in 1997. We had no engagement to assist SaskPower in the sale of Channel Lake.

We became aware in January 1997 that SaskPower wished to sell Channel Lake. On February 4, 1997 we introduced Mr. Ken Christensen and Mr. Murray Black, both of SaskPower, to Mr. Don Stewart, a partner in our Calgary corporate finance practice. Mr. Christensen was seeking our views on SaskPower's options available to sell Channel Lake.

On February 12, 1997 Mr. Stewart issued a proposal letter to SaskPower offering to act as financial adviser to SaskPower in the sale of Channel Lake. Ernst & Young Corporate Finance Inc. was not engaged to perform that assignment.

Item (7): our engagement with Channel Lake subsequent to the sale of the company by SaskPower. In early June 1997 we were contacted by Mr. Portigal who informed us that Direct Energy's parent, OPTUS Natural Gas Distribution Income Fund, herein referred to as OPTUS, had completed a special warrants financing to raise the proceeds that were used by Direct Energy for the acquisition of Channel Lake from SaskPower.

In that regard, Mr. Portigal noted that OPTUS was required to file a prospectus with securities regulators across Canada to qualify the special warrants for conversion into freely trading trust fund units. Mr. Portigal indicated to us that Mr. Bill Maslechko, a securities lawyer at Burnet Duckworth & Palmer, would be contacting us to discuss The Securities Act requirements for disclosure of Channel Lake information in the OPTUS prospectus.

In early June 1997, Mr. Maslechko informed us that the various provincial securities regulations would require that the OPTUS prospectus include the audited historical financial statements of Channel Lake for the three years ended December 31, 1996 together with unaudited interim financial statements of Channel Lake for the three months ended March 31, 1997 and 1996.

We confirmed to Mr. Maslechko that it was possible to prepare

such unaudited interim financial statements but that we would seek the approval of SaskPower to do so. At the same time, we were asked by Mr. Portigal to complete the review — for purposes of the OPTUS prospectus — of the March 31, 1997 and 1996 unaudited interim financial statements for Channel Lake, and to assist in the preparation of the three-year historical audited financial statements for the company.

Before commencing any work we contacted Ms. Hall at SaskPower and inquired whether SaskPower were aware of any reasons why we should not complete the engagement and asked that Ms. Hall inquire with other SaskPower management as appropriate. We were informed that there were no objections to us completing the work. We commenced our review procedures in mid-June 1997 and completed those in the latter part of June 1997.

OPTUS filed its preliminary prospectus dated June 26, 1997 with securities regulators across Canada. The prospectus included the financial statements of Channel Lake as described above. We provided a comfort letter to the securities regulators on those financial statements. Prior to providing the comfort letter, we inquired again with Ms. Hall and asked her to confirm with SaskPower management that they had no objections to the Channel Lake historical financial statement appearing in the OPTUS prospectus.

Ms. Hall confirmed with us that she had made appropriate internal inquiries and that there were no objections to the inclusion of the Channel Lake financial statements in the OPTUS preliminary prospectus. We made these inquiries of SaskPower because we were not aware of whether Channel Lake financial statements had been tabled in the legislature and because prospectuses, such as the one to be filed by OPTUS, are public documents.

During our review procedures completed in late June 1997, Mr. Portigal indicated to us that there was an issue between Direct Energy and SaskPower with respect to the manner in which trading losses were to be funded by SaskPower in the Channel Lake purchase and sale agreement. He also told us that he believed SaskPower's concerns had been resolved. He did not mention that there was a concern that the purchase price had changed. SaskPower did not inform us at that time that they had a concern.

On August 21, 1997 OPTUS filed a final prospectus with securities regulators across Canada and we issued the required consent and comfort letters to the various securities commissions. Again, at that time, we confirmed with Ms. Hall at SaskPower that SaskPower had no objections to the inclusion of the Channel Lake financial statements in the OPTUS prospectus.

Item (8): our audit of the 1997 financial statements of SaskPower. During March 1997 we had an initial discussion with personnel in SaskPower's finance group regarding the accounting treatment of the sale of Channel Lake in the 1997 consolidated financial statements of SaskPower. The focus of that discussion centred around hypothetical figures for proceeds and the mechanics of calculating a gain or loss on sale of shares.

As part of our 1997 audit plan, which was discussed with the audit and finance committee in November 1997, we identified that we would have to examine the accounting for the sale of SaskPower's investment in Channel Lake.

We had further discussions with personnel in SaskPower's finance group in January 1998 in connection with the 1997 year-end audit of SaskPower. These discussions focused on the reporting of the results of a discontinued operation up to the date of disposal and the separate accounting for the gain or loss on disposal of the shares. Guidance for accounting for discontinued operations is found in *CICA Handbook* (Canadian Institute of Chartered Accountants) section 3475. SaskPower's 1997 accounting for Channel Lake followed the *CICA Handbook* requirements.

During the course of our audit we reviewed the Direct Energy Gas Supply Agreement. As is common with any long-term agreement, we wanted to understand the substance of the agreement and ascertain whether the company's proposed accounting treatment would be in accordance with generally accepted accounting principles.

Many long-term purchase or sale contracts are simply recorded as expenses or revenues over the course of a contract. However, in some instances, due to the facts surrounding particular contracts, it is more appropriate that the accounting treatment not mirror the timing of the cash flows in order to provide a better reflection of the economic substance of the transaction.

In the case of the gas supply agreement, there was no upfront cash receipt or payment. It is structured as a cost-plus-management-fee-type of contract, with the management fee calculated by way of a sliding scale percentage of purchases depending upon volumes of gas purchased. In reviewing this contract, we wanted to establish whether the management fee constituted a reasonable market rate within reasonable materiality limits.

If the rates were significantly in excess of normal market rates, it might have been appropriate to assign a value to the contract by recording a deferred amount at the time of signing the contract equal to the discontinued future excess charges. Such a deferred amount would be amortized over the life of the contract. The fact that Direct Energy may earn a profit over the life of the gas supply agreement does not in and of itself suggest that a value for accounting purposes needs to be ascribed to the contract at the time of signing.

To assist in our audit of SaskPower's accounting for the contract, we sought the views of Mr. Gordon Graham, a partner in our Calgary office who has experience with gas supply and marketing arrangements. Other than the fact that the agreement covered a period longer than others he had seen, the financial terms of the agreement did not, in his view, suggest that the management fee in the agreement was significantly different from market rates.

We considered the fact that the agreement stipulates SaskPower is not obligated to buy any minimum annual, monthly or daily volumes of gas. We also gave consideration to the Direct Energy management fee that would be incurred by SaskPower based on estimated levels of gas consumption set out in the gas

supply agreement using then current gas prices. Assuming that the amount of the management fee would not be a pure profit to Direct Energy, given that Direct Energy had a number of operational and administrative requirements to meet under the agreement, the discounted amount of future payments did not cause us to suggest that SaskPower should have accounted for the transaction differently.

Taken together, our internal consultations and our analysis suggested that there was no need to record any deferred amount in 1997 in respect of the gas supply agreement for accounting purposes, and that SaskPower should account for any costs under the agreement in future years when such costs would be incurred.

Madam Chair, this concludes our opening remarks. Mr. Munro and I will be pleased to answer the committee's questions. To assist the committee in determining which of us may be best able to answer your questions, I can best address the issues with respect to SaskPower, including communications with SaskPower management and the audit and finance committee; Mr. Munro can best address the issues with respect to Channel Lake and our audit of that entity.

Thank you.

**The Chair:** — Thank you, Mr. James. I'm sure that all committee members appreciate the thoroughness of your opening statement. It has certainly helped us to formulate questions.

I would ask committee members now at this time, did you wish to have a brief recess? I rather assumed that so I think what we will do is . . . Will 15 minutes be sufficient? Then we'll have a 15-minute break; we will resume at 10:15. The committee is recessed until 10:15.

**The committee recessed for a period of time.**

**The Chair:** — If Committee members would take their seats please. Mr. Gantefer, are you ready?

**Mr. Gantefer:** — Thank you very much, Madam Chair.

**The Chair:** — Until approximately 10 to 11, please.

**Mr. Gantefer:** — Thank you. First of all, Mr. James and Mr. Munro, welcome, and I would like to compliment you on a very comprehensive report. It certainly was comprehensive enough that we had to review our questions to see which items were still relevant and which were perhaps already answered in your report.

I would like to go over . . . I think what I will follow to some extent is . . . The organization of your report probably makes it easier for us to go through it and try to incorporate some of the issues that we had.

First of all, you make reference in your reports to the management letters and I wonder, in general, is a management letter — not specifically in this instance but as part of your normal work — are management letters pretty common occurrences as attachments to financial statements?

**Mr. James:** — Well I can answer that . . . First of all, thank you for the comments on the report. Our intent was to be as complete as we could and try to anticipate the key areas that you might be interested in and the areas that we knew something about.

To answer your question, a management letter is one tool that we use to communicate. We occasionally will deal with an issue or notice an issue or an item that we feel that we should recommend to a client. It can be communicated verbally; it can be communicated in a letter, if there's a certain amount of detail that we want to communicate.

And in fact it's becoming more and more common with larger organizations to simply do an electronic PowerPoint presentation to a group of management or a group of a board without going to all the trouble of doing a, you know, two- or three-page letter. The idea is to communicate.

When we're doing . . . when we're engaged to do an audit, we're engaged to do the audit of the financial statements. We're not engaged to issue the management letter. It is an offshoot. So I hope I've answered the question. There are really various different ways that we might do it. A written letter is not always the way that it's done.

**Mr. Gantefer:** — Would it be accurate at all to say that there may be different levels of how you — and different seriousness of the issues that you raise that — would determine to some extent what technique you would use to communicate this. For example, if it is a minor item, you may just sit down verbally and have a chat about it and have it resolved that way. If it was of somewhat more significance that you wanted a broader group of people to see, perhaps a PowerPoint presentation might be there.

But if you wanted to formalize a concern, and so there's a paper trail and a greater significance of the issue, then in those instances perhaps you would restore or resort to the management letter as a tool to communicate the concern?

**Mr. James:** — Yes, I would say that pretty fairly sums up the alternatives and the situation in which we would issue a letter. As well, one has to have an appreciation for one's client. I mean some clients prefer perhaps a more formal process, others would prefer simply to have a discussion with a group of people around the room. So you have to read your client situation as well. But again, our objective is to communicate information, not to be bureaucratic about it.

**Mr. Gantefer:** — So then when a management letter is written, it likely would have been preceded by verbal communications, discussions with key management people about the concerns raised in the management letter or what were going to be raised in the management letter. And by the fact you appended a management letter to the document indicated that you wanted this on the record, and that it then was the intention of your audit firm to make sure that these concerns were documented and potentially transmitted to the respective authorities, boards of directors, etc., in that nature.

**Mr. James:** — Yes, I think I heard two questions in there. The first would be yes; there are verbal discussions, often quite

extensive. You have to understand as well that when one is doing an audit of a relatively . . . well any size organization, there are several people involved — junior people, more intermediate people, senior people such as ourselves. Often an issue will be raised by someone out there doing work on the cash or the accounts receivable or inventory or whatever. They'll raise an issue. They'll make a handwritten note or type it into their computer.

When we get to the end of the audit, we sit down with our staff and assess what issues have been raised. Sit down with the appropriate level of management, and sometimes we discover that we've gone up a blind alley. I mean there's an issue there that really isn't an issue once you talk to the right person and you discover that a particular item is not . . . is already being dealt with but in another way.

So yes, there are discussions; yes, the way things are worded will be changed when you understand more facts and you inquire. It would be quite irresponsible of us, actually, to issue a letter strictly to the president and the audit committee without having had discussions with the right people because we could end up looking foolish if we had not understood all the facts.

So that's the first part of the question. The second part of the question is . . . I'm sorry, I've forgotten what it was.

**Mr. Gantefoer:** — The intent of the management letter to make sure that the issues you raise get to the boards of directors or the proper authorities over and above the management.

**Mr. James:** — Yes.

**Mr. Gantefoer:** — Thank you. In your management letter, you indicate a concern about the fact that Channel Lake is undertaking gas trading programs. And I believe that initially you were concerned that they were being done without proper authorization, went beyond the guarantee of supply and security of price that the original authorization had been, and that there were not proper accounting and procedural mechanisms in place to allow this to happen appropriately. Is that correct?

**Mr. Munro:** — I think you sort of asked two questions. The question about whether it was within the original mandate, I'm not sure that we can turn our attention to because I really think you have to go back to that mandate question and ask a SaskPower board member what they meant when they said security and supply.

In respect of Channel Lake, the board of directors of Channel Lake had given Channel Lake, the company, the approval to go do tender into gas trading programs. Our management letter really sort of directed its attention to saying, if you are going to go do that, be certain that you're establishing proper procedures and policies and reporting to ensure that you govern that process properly.

**Mr. Gantefoer:** — So that in your management letter you indicate that they had been given the authority to engage in gas trading activities. Was that authority given by the Channel Lake board of directors then?

**Mr. Munro:** — That authority was given by the Channel Lake

board of directors.

**Mr. Gantefoer:** — Did you explore if the Channel Lake board of directors had that authority from the SaskPower board of directors who ultimately were the owners of Channel Lake?

**Mr. Munro:** — No.

**The Chair:** — Excuse me that might not have been caught on the record. Your answer, Mr. Munro?

**Mr. Munro:** — My answer to his question . . . my answer was no.

**Mr. Gantefoer:** — Thank you. So you only dealt with the aspect from the Channel Lake board which you recognize of course were all SaskPower employees.

**Mr. Munro:** — I recognize they were senior management of SaskPower, correct.

**Mr. Gantefoer:** — In your concern . . . you expressed concerns over a period of time that there weren't the control mechanisms in place in order to safeguard Channel Lake and ultimately SaskPower against potential losses.

Was it, or is it normal for I think somewhere in the order of two years to go by and really know . . . I don't detect from your report that there was significant improvement in regard to these concerns over a fairly long period of time. Is it normal that such inaction is a result of a management concern that you've raised?

**Mr. Munro:** — No, I think it would be . . . a number of our concerns continued throughout the two-year period. I think it would be fair to say that Channel Lake itself built systems of controls and procedures over that period, particularly with respect to the oil and gas operations. Our 1993 management letter really spoke to the period of time in which the company was originally formed. And it would be fair to say that a number of our comments there really spoke to how they were accounting for the debits and credits surrounding the oil and gas operations. And, as the company evolved, it continued to build controls, but that didn't sort of lessen our concerns, as communicated in our management letters about continuing to put those systems in place.

**Mr. Gantefoer:** — Is it normal in your experience when you raise those concerns that the company you raise the concerns with would be so slow in addressing the concerns?

It would strike me as that if my auditors had issued some concerns about how I was practising business that it's sort of a thing you put to the top of your priority and say, I better take a look at this and deal with it very quickly. It seems that there was not a lot of haste demonstrated in terms of getting these controls in place. It was an on-going two-year process.

**Mr. Munro:** — Yes, I guess there's two-fold things. In respect of the oil and gas operations, I think the company did a thorough and adequate job of establishing systems and procedures to account for their oil and gas operations and to sort of safeguard those assets. In respect of the gas trading, our comments remained because the company developed draft

policies and didn't move to putting those fully into place.

I do recollect during the period of time, and when Mr. James and I spoke — our opening statement speaks about reviewing draft policies — and during that point in time SaskPower was attempting to develop its own strategies with respect to kind of risk management. And we're looking for sort of input, and trying to decide on sort of a broader risk management committee. So I think the draft policies got built by the Channel Lake level and then got to that sort of broader SaskPower level, then stopped.

**Mr. Gantefer:** — On page 9 of your document you talk about the fact that trading losses were first disclosed or first happened when you were doing an audit in November of 1996 where the two companies, Multi Energies and NESI, were going bankrupt and that put Channel Lake into the position of being into trading losses.

You indicate, I believe, that you discussed this with SaskPower's finance group management and the staff of the Provincial Auditor at that time. Who would be the people on the SaskPower's finance group management?

**Mr. Munro:** — That information would have flowed up through I guess your audit, Rupert, and would have primarily been Pat Hall and Rob Spelliscy, and up through Ken Christensen. I believe, in respect to the Province Auditor, the Provincial Auditor representative was Ed Montgomery.

And the process that they use is that review . . . I mean they audit alongside of us, if you like. They review our planning files and sign off on our planning before we actually execute our year-end procedures.

In respect of Channel Lake, we would provide all of our files from Calgary to them. They would review those files and come back to us to discuss all of the significant issues so that they were apprised of the issues and made sure that they were satisfied that we were executing the procedures that they in turn would if they were doing the work themselves.

**Mr. Gantefer:** — Did you discuss at that time any of these concerns with the audit and finance committee of SaskPower?

**Mr. James:** — I don't recall any discussions at the November time period. The discussions that took place happened . . . it would have been at the . . . There were usually two meetings of the audit and finance committee, perhaps is the best way to answer this — one at the planning stage where we present an audit plan to the audit and finance committee, and then following the completion of the audit there's another meeting. And at both of those meetings the Provincial Auditor and/or his staff attend, and at the closing meeting management discusses what's in the financial statements and we add comments, as we feel necessary. And also the audit and finance committee — that corporation have typically had an in-camera session also with the auditors without management present.

So the discussions that were held on this issue would have been held at the spring meeting following the completion of the audit work.

**Mr. Munro:** — Likely because the gas trading losses, I think it's either NESI or Direct, I don't remember which multi-energies filed for bankruptcy right in late November — I think the records have something around November 26 as likely — after the period of time in which Rupert had had his fall 1996 audit planning meeting with the finance committee.

**Mr. Gantefer:** — So the discussion that you would have had about the potential trading losses occurred with the management group but never happened with either the audit and finance committee or any board members. Is that correct? Until after the spring meeting or . . .

**Mr. James:** — Yes, until the . . . and that's the usual time when you sit down and go through items that you've seen or concerns you might have or questions or whatever. It's typically more at the end that that discussion takes place. The planning meeting is really focusing on those issues at that date that one is aware of already.

**Mr. Gantefer:** — On page 10 of your opening statement, you indicate that on March 13 you met with Mr. Portugal to discuss the determination of the trading losses and he indicated to you that he was in the process of attempting to sell Channel Lake. Was that the first time you heard about the proposal to sell Channel Lake?

**Mr. James:** — No the first time would have been under item 6, where the comment: "we became aware in January of 1997 that SaskPower wished to sell Channel Lake". That was the first time that we had heard that there was a desire to sell the company. And it was at that time that I . . . that Mr. Christensen said to me, do you have anyone in Calgary who might be able to help us? So I put him in touch with Mr. Stewart and Mr. Stewart dealt with it from there.

I didn't have any further discussion on that other than one conversation later on with Mr. Stewart when he phoned up to say, have you heard anything on our proposal. That was the only other conversation I had on it. And then this comment really in the narrative, Mr. Portugal indicating he was in the process of attempting to sell Channel Lake and that was really your . . .

**Mr. Munro:** — The first time that I was aware of it, we were aware that they were contemplating selling the company, was the first time I was aware that Mr. Portugal was sort of acting as agent, for lack of a better term, to execute that transaction. I did participate in the February meeting with Mr. Stewart, Mr. Christensen, and Mr. Black. So I was aware that Ernst . . . finance had proposed to assist the company. I was also aware that we weren't engaged to do that.

**Mr. Gantefer:** — In leading to the fact that you contacted Mr. Stewart as your expert in terms of a proposal, who first made you aware then that SaskPower potentially wanted to sell Channel Lake?

**Mr. James:** — I believe it was Mr. Christensen in January when he commented in that January that we'd like to sell this company, do you have anyone who could help us?

**Mr. Gantefer:** — Okay, so do you know if that would be

early, late January or roughly the time line?

**Mr. Munro:** — The meeting happened sort of very shortly after Rupert called us and the meeting was held February 4. And the proposal I think was dated February 12.

**Mr. James:** — See you also have to realize that that is the time of year when we were doing the year-end audit for SaskPower so we've got a staff in there working. I'm over there every other day or whatever reviewing a file or attending a meeting or discussing something with my staff. And he caught me one day and saw me and he said well come in and I got to tell you something or ask you something. Do you have anyone in Calgary that knows anything about disposing of companies? And that's what started the process.

I said certainly I can place a phone call and get you in touch with someone. So that's when I heard and it would have been late in January or it could have even been early February I suppose, but . . .

**Mr. Gantefer:** — In the proposal that was made to Mr. Christensen subsequent to that meeting by Mr. Stewart, document CPL 13/22 goes through the proposal that you refer to under item 6. The proposal letter as it was dated, as you indicate February 12; I think goes through a lot of technical stuff.

On page 2 near the end, under the process, it says that there's two options for marketing the company, and I quote:

. . . can be done in two ways. The first option is a broad distribution in the market-place of this opportunity. This may produce the best price and take the longest period of time, however you have eliminated this option.

At the earlier meeting that you had, was it discussed in terms of the importance of the March 31 deadline? Was that discussed and is that why this elimination of the . . . the first option was eliminated?

**Mr. Munro:** — My recollection is that there was a discussion that time was of the essence. And that a full sort of public marketing where you opened a data room — which is normal in the oil and gas industry — opened a data room; you sort of advertise that people can come and look at your properties. That wasn't sort of the desired approach.

And I think Mr. Stewart's comments here were to point out that there is more than one way to do the process and he was sort of eliminating that one.

**Mr. Gantefer:** — I don't think he was eliminating; he was suggesting that it was prior . . . it was eliminated by SaskPower.

**Mr. Munro:** — That's correct.

**Mr. Gantefer:** — When you say that time is of the essence, does that speak to the issue of how the reporting was going to happen on the March 31 deadline? Being the auditors for SaskPower, you would of course understand the significance of March 31.

**Mr. James:** — Well the significance of March 31 is that The Tabling of Documents Act, if I'm not mistaken, requires that the financial statements be tabled within I believe it's 90 days following the fiscal year end of the company. And then there's some special rules in there as to whether the House is sitting or not, and I always have to go and look at it to refresh my memory on the specific rules.

To my mind the March 31 date, from an accounting perspective in SaskPower, has never been a very significant date for me. The reason I say that . . . And we alluded in this document to the accounting standard that one must follow when you're disposing of a part of your organization, and that is called "discontinued operations". And whether this was sold on January 31, February 28 or 29, or March 31, or sometime thereafter, one would still look to that guidance to do the accounting.

So I've never quite understood why people are assuming that March 31, having . . . that the March 31 date would specifically affect the accounting. Yes, it certainly could affect the tabling because I would assume if one had sold the company, say on March 25, that one could say to the legislature, we don't have anything to table because we sold the company. But I've never understood this issue that people have been talking about in the testimony about why the March 31 date would affect the accounting. And I can direct you to that standard and you can read it and understand what I'm saying.

**Mr. Gantefer:** — If there were trading losses incurred in the year ending March 31 in any given year, would those be able to be offset by sale of asset shares and consequently the amount of the trading losses would be diminished to some extent by a gain on the sale of shares?

**Mr. James:** — All right, the accounting standard for the disposal of discontinued operations requires the disclosure in the financial statements of certain things. One being, what is the gain or loss on the sale of the shares when you sell them? The other is what is the results of operations of that organization from the beginning of the fiscal year until . . . I'll simplify this by saying the date of sale? I mean there are some other rules that you could fall into but I'll say the date of sale, all right. So it is required to disclose those as separate items; it's very clear in the accounting standard.

The only time that one might not see those and you . . . I mean these financial statements because they're dealing with billions of dollars . . . I mean they are to the million-dollar amount. So if the amounts happen to be relatively small, you know, they might not be shown — if the amount was quite small.

But in fact if you look at the 1997 annual report, the financial statements therein, you will see two lines on the statement of operations. One is the loss from operations from January 1 to the date of sale and the other is actually an accounting gain on the disposal of the shares. One is a \$3 million minus; the other is a \$3 million plus. They happen to net but that . . . Sorry, they happen to be the same number, going in different directions. They haven't been netted. The accounting standard in fact does not allow one to net them, unless of course they were very small.

**Mr. Gantefer:** — When you go to consolidated financial statements at SaskPower level though how would they be reported?

**Mr. James:** — Well I'm talking about . . . I'm talking about . . .

**Mr. Gantefer:** — So they'd be a net.

**Mr. James:** — And I'm talking about the consolidated statements, and the thing that's important to understand in this — and I know this has come out in previous testimony also — is that if you look at the years 1993 through 1996, there was no discontinued operation in any of those years.

This subsidiary, along with any other subsidiary, is consolidated into SaskPower and that's why they're called consolidated financial statements. And note one in each one of those years has disclosed the existence of Channel Lake, along with other subsidiaries listed in note one.

The thing that's different about 1997 is that you now have a discontinued operation during that year. Therefore one must look to the recommendations in section 3475 of the *CICA Handbook*, which specifically says that you must break out of those consolidated financial statements, the numbers — certain numbers — related to the business that you're selling.

And that would include gain or loss on sale of shares; it would also include gain or loss on the operations of the business. It also requires you to break out the revenue I believe, and the key assets of that business.

And again if you look at — and I can refer you to the note if you like — you will see it in the note to the 1997 financial statements. Am I making myself clear? That's the difference between pre-'97 and '97.

**Mr. Gantefer:** — In the minutes of the meeting in Calgary on February 4, document CLP 13/21 . . . I refer you to them. And that's the meeting where SaskPower and Ernst & Young talked about the disposal of the assets of Channel Lake. At the second last paragraph, I would read into the record. It says:

If we want to look at selling Channel Lake there may be a way of erasing some of the trading losses that we are anticipating. If we write a contract with the eventual purchaser of the Channel Lake assets, for the purchase of natural gas from the Channel Lake assets, we may be able to get a higher price for the assets and thus offset the trading losses we will see.

If there was not this balancing potential, why was that paragraph inserted in the minutes?

**Mr. Munro:** — For the record, the first occasion I've had to see the minutes was last week in preparation for our attendance. I think the minutes are drafted by Mr. Black of SaskPower and certainly didn't have the approval of us.

I was in attendance at the meeting. I think Mr. Stewart talked about an appropriate potential purchaser for these types of assets, and given that SaskPower had a natural gas requirement, he might be to find the type of purchaser who could make use

of the production off the assets but also supply natural gas. And that in respect of the trading losses, I think Don's only comment was at the time that one needed to do a proper analysis of the trading losses to see whether there was an opportunity to minimize the losses through some sort of creative bundling of the products.

But that was really sort of an attempt to realize the greatest aggregate proceeds for the sale of the assets, and at that meeting there was never a discussion about whether that should occur, whether it was feasible to occur, or whether that would influence the accounting or financial reporting.

**Mr. Gantefer:** — So are you indicating that this section is misleading in terms of the impression it leaves a reader?

**Mr. Munro:** — From my perspective it is.

**Mr. Gantefer:** — And the minutes were prepared by Mr. Black of SaskPower?

**Mr. Munro:** — Well I presume they were because I'm also aware that there were also notes from Mr. Christensen somewhere in the same binder of material that we came across, and I had not sort of seen those until, as I said, in preparation for this last week.

**Mr. Gantefer:** — I can very much appreciate your explanation from an auditor's standpoint but it strikes me as, if there is a clear perception on SaskPower that there is the ability to, as it says, erase some of the trading losses if this transaction occurs on or before March 31.

**Mr. Munro:** — No I don't think . . . Again being in attendance at the meeting, I know that the discussion specifically took place. Mr. Stewart indicated that in his initial assessment that the optimal type of purchaser for these assets, given that SaskPower also had a natural gas purchase requirement, that you would identify those entities who might like a physical supply of gas to support their gas trading activities. You might bundle SaskPower's requirements along with the sale of the assets, and in respect of the trading losses, do an analysis to determine whether there is a best way to mitigate the amount of losses occurred rather than just going and closing them out in the open market. And in that way package the product in such a way that you might realize the greatest price.

That's the discussion that happened. There was never a discussion about if you do all of this, gee; you could kind of bury it from the public eye.

Mr. Stewart wouldn't have been in a position to ever make that assessment anyway because his expertise is in corporate finance and buying and selling companies, not in sort of audit matters.

**Mr. James:** — He also doesn't have any background specifically in the kind of the reporting structure that goes on in this particular province with Crown corporations.

**Mr. Munro:** — He'd never met with Christensen before.

**Mr. James:** — I mean he didn't sort of have a background. Coming at it that way, he was simply discussing it as a potential

adviser.

**Mr. Gantefer:** — Make no mistake. I'm not suggesting Mr. Stewart was suggesting this. He was being told from the suggestions on February 12 that March 31 was the date. He wasn't suggesting that that date would play to some advantage at all in his recommendations or from his expertise, so I'm not at all questioning his perspective in this.

What I am trying to get to is that March 31 was much more than a tentative date taken off the wall because it precludes Mr. Stewart's first recommendation which says that if you want to do this for the best results, you take some time. You do it in the normal course of events.

**Mr. Munro:** — In respect of the March 31 date, and again my answer now has I guess been influenced by sort of all of the previous testimony that I've sort of read and the various reports, and so I'd have quite a bit less appreciation of the date at the time. Because I don't believe at the time when I was in that meeting that I was even aware of the requirements for a subsidiary of a Crown corporation to table within 90 days. I mean I knew that Crown corporations tabled in the legislature.

But I think that our answer at that meeting was that if you are picking a March 31 date, that is an aggressive timetable, and you're going to have to sort of change your course of action to meet that or sort of pick a particular course of action.

And there was never any contemplation by Rupert or I — and we reflected on this subsequent to the period of time of '96-97 largely because it's been sort of an issue at these hearings — that we'd not have ever changed our opinion about what the appropriate accounting is. And the appropriate accounting is that there's no way in our view that you could have hidden or netted the trading losses against any gain on sale of Channel Lake and prevented it from becoming sort of matter of the public record, whether the date was March 31 or anything other than that.

**Mr. Gantefer:** — And again I'm not suggesting that March 31 was your suggestion or your firm's or Mr. Stewart's or anyone's.

But certainly March 31 was a significant date from SaskPower's standpoint because it automatically, according to Mr. Stewart's report, eliminated the first option, which was the best option in his opinion. And it said basically that you've eliminated it, because of March 31, you being SaskPower. Not your firm . . .

**Mr. Munro:** — Right. And I can't add anything more to that being in the meetings and sort of participating in all the other meetings subsequent to that. Clearly March 31 became a significant date and I can't add any further insight to whether . . .

**Mr. Gantefer:** — Thank you. I would like to cover one other area and that is the area of the sale price of 20.8. You received the document . . . you indicate the document dated April 2. Is that the same document that talked about a net price of 20.8?

**Mr. Munro:** — The document we received on May 5 was a

signed purchase and sale agreement dated May 2 which has a purchase price of \$20.8 million as we reported in our opening statement. I was not aware that there were sort of various versions of this agreement that sort of now have been discussed.

I can tell you that we also obtained in the process of doing our March 31, 1997 unaudited review of the financial statements that went into the OPTUS prospectus that we discussed, we obtained directly from the Burnet Duckworth closing binder another copy of that purchase and sale agreement. And in preparation for these hearings again last week we compared the three paragraphs that seem to be the paragraphs of question, and they were the same.

**Mr. Gantefer:** — You indicated as well you didn't receive any of the four or so memos that Mr. Portugal had sent over. Would it be normal practice for you as the auditors to receive that kind of information?

**Mr. James:** — Not normally. Typically, unless a client says to you we are about to engage in a particular transaction, would you sit down with us and, you know, help us or look through the documents or whatever, which is really what Mr. Stewart's offer was to do, his proposal was to do. But in companies like SaskPower, and all of our other clients do all kinds of agreements all the time.

And typically what happens is you come in to do your audit in the fall or in the winter and you say, well you sold this. We need a copy of the agreement. If it's not signed we say will you give us a signed copy. I mean that's then . . . we start from there and we tie that in to what they've done in their accounting.

So I wouldn't have expected Mr. Portugal to — I'm sorry I lost my train of thought — I wouldn't have expected Mr. Portugal to have provided us with copies of the documents nor management, not at that time. And in fact we didn't know about these documents until they came out in the committee hearings you know, so it's not normal practice just to give us documents.

**Mr. Munro:** — Just because they were specific documents dealing with sort of the changes of draft agreements, and we weren't involved in the sale process or providing any advice with sort of the mechanics of the sale, they just weren't sort of relevant documents to us. They clearly were relevant to others.

**Mr. James:** — We don't actually care how many drafts there are of an agreement. There could be one; there could be 101. What we want to see is the final signed agreement and then the accounting falls from that.

**Mr. Gantefer:** — Except that you were asked to prepare a subsequent event note that disclosed the sale price.

**Mr. James:** — Right.

**Mr. Gantefer:** — And you did that based on the document that you received at 20.8.

**Mr. James:** — That's right.

**Mr. Gantefer:** — And we now know that those memos if you like, and subsequent drafts significantly changed the sale prices.

So in a way, you had to give an opinion by the way of a subsequent event note on the basis of not having all the information.

**Mr. Munro:** — I'm not sure that my . . . No, I am certain that my subsequent event note would not have changed had I had all of those memoranda because I specifically chose the sale price out of the clause of the agreement being the relevant sale price as sort of disclosed in the signed purchase and sale agreement. And when you go to the other significant clause within the purchase and sale agreement being clause 6.3 which deals with sort of the gas trading losses, it was not clear to me at the time how sort of mechanically they would make that process work because that agreement talks about SaskPower establishing an account to deal with the trading losses. And I wasn't certain of whether that would be pushed as an obligation of Channel Lake to fund or SaskPower or anything. So the number would not have changed. The number would not have changed had I saw Mr. Portigal's memos.

**Mr. Gantfoer:** — So you still believe that SaskPower had reason to expect they were going to receive the net price of \$20.8 million from the sale of Channel Lake?

**Mr. Munro:** — I can't answer that question because I think you have to address that to the SaskPower officials. When I read the agreement, I understand that the purchase price is \$20.8 million subject to certain adjustments as specified in the agreements. I do understand in their meeting of March 13 with Mr. Portigal, I was under the understanding that there was going to be a mechanism in place where Channel Lake or SaskPower would fund the trading losses and indeed that's what the agreement says.

**Mr. Gantfoer:** — Thank you, Madam Chair. I could continue but I've overstayed my welcome.

**The Chair:** — I wouldn't put it quite so harshly but I do appreciate the fact that you will now yield the floor to Mr. Hillson.

**Mr. Hillson:** — Thank you, Madam Chair. Good morning, gentlemen. Now you say that in your view there is no magic in the March 31 date in terms of what is required to be reported to the legislature.

**Mr. James:** — In terms of the accounting, that's what I said.

**Mr. Hillson:** — And in the 1997 report of Saskatchewan Power there is a discontinued operation accounting provided on page 41, along the lines of what you testified to this morning, and that does in fact show accounts payable and accrued liabilities of 14 million.

**Mr. James:** — That would have been their normal . . . the company's regular accounts payable and accrued liabilities at December 31, 1996, yes, their trade payables.

**Mr. Hillson:** — So that's where we see the trading losses is it, in that figure?

**Mr. James:** — No.

**Mr. Hillson:** — Where would we see the trading losses?

**Mr. James:** — The trading losses are disclosed in the notes to the Channel Lake financial statements. The trading losses to the tune of \$2.4 million were included in 1996 in the Channel Lake income or loss, whatever that might have been.

**Mr. Hillson:** — Those weren't published though, were they?

**Mr. James:** — I don't believe so, but those form part of the . . .

**Mr. Munro:** — The \$2.4 million loss is reflected in the net profit of SaskPower for 1996 through the consolidation process.

**Mr. James:** — Right. But the trading losses subsequent to December 31, 1996 were a contingency, which is what's disclosed in the Channel Lake financial statements — SaskPower has a contingency note. It does not specifically make reference to the trading losses.

Consideration was given at the time. In fact we discussed it in terms of sort of what's the downside on that number — how big could that number get, would it become material to SaskPower in terms of the need to disclose it. And we concluded that the amount of disclosure on contingencies in these financial statements was sufficient, given the fact that that \$5.6 million estimate did not appear to be a number that could be growing and growing.

And any organization like SaskPower that is running quite a risky business in terms of dealing with steam and power lines and all of the things that go along with that business always have contingencies. It's a question of how significant it is and whether it needs to be mentioned.

**Mr. Munro:** — For clarification, the 1997 financial statements of SaskPower would reflect \$3.1 million of gas trading losses that were incurred by Channel Lake during the period of time in which SaskPower owned Channel Lake prior to the sale date.

**Mr. James:** — You can see that number on page 33, the consolidated statement of income and reinvested earnings. If you look about three-quarters of the way down you'll see a net loss from discontinued operations minus three. That includes the results of Channel Lake for the part of 1997 that it was owned by SaskPower, okay?

Now that three happens to be the same number as the 3.1. But I mean there were other income and other expense items, you know, in that period of time, but the net happened to be three. So the 3.1 was picked up in this column here and the remaining amount of the 5.6 is a contingency which carries forward. And so the difference would be 2.5, which is a remaining contingency that would affect SaskPower.

So anyway, in terms of 2.6 in relation to an organization that has already liabilities of \$2.2 billion, I mean it just isn't a number that would typically be broken out anywhere.

**Mr. Hillson:** — So is there anywhere though in this annual report though that I could find trading losses for Channel Lake?

**Mr. James:** — No.

**Mr. Hillson:** — No. And is there anywhere that I could find: this is our total experience with Channel Lake in terms of how we did, how much it would cost us to acquire it, how much we sold it for, what our trading experiences were during its operations?

**Mr. James:** — No, the note 5 factually indicates that they sold the subsidiary. The rest of the annual report we do not audit. The rest of the annual report management prepares. We do review it for internal consistency — make sure that it's reasonable in terms of the words that are mentioned — but the auditor's report is strictly on the financial statements. Financial statements contain the required disclosure.

It's management's choice as to how much they want to say about anything that goes on in the company, you know, in terms of their experience. You know I don't sort of second guess that, especially on a transaction like this.

**Mr. Hillson:** — So you provide management with the information. How much or how little they choose to report publicly is then a management decision.

**Mr. James:** — No, it's the opposite way around. Management prepares the financial statements and management prepares the rest of the annual report. The auditor's job is to audit the financial statements prepared by management. Okay? So if we . . .

**Mr. Hillson:** — And provide an opinion on them.

**Mr. James:** — And provide an opinion on them.

So our responsibility is to be satisfied or otherwise, whether the financial statements fairly present the results of operations of the corporation, and our measure, our benchmark, for that is generally accepted accounting principles. And that's what the auditor's report says.

**Mr. Hillson:** — But I guess my question is, though, that if a board member or a member of the public wanted to simply know how did we make out over Channel Lake, could they read this annual report or any other annual report and find out?

**Mr. James:** — They could find . . . they could most certainly find out the information that's disclosed in 1997. They would discover that there is a loss from operations for the period owned and they would discover the other information that is there. There's no other story or other words to explain anything more about the scenario, no.

**Mr. Hillson:** — Okay so they would find . . . we would find loss from operations during period owned?

**Mr. James:** — Correct.

**Mr. Hillson:** — Okay and where would we find that entry, sir?

**Mr. James:** — It's on page 33 — net loss from discontinued operations, \$3 million.

**Mr. Hillson:** — Okay. So we'd find a \$3 million loss from discontinued operations. Now there isn't a reference to Channel

Lake there. I thought you said that that's not just Channel Lake, or is that only Channel Lake?

**Mr. James:** — That's only Channel Lake.

**Mr. Hillson:** — That's only Channel Lake.

**Mr. James:** — And you'll see beside it, it says note 5 and then note 5 is the note we've been talking about on page 41 that specifically says that "... the Corporation sold its wholly-owned gas supply subsidiary, Channel Lake (etc.) . . ."

So I mean it's . . . I believe it's clear that Channel Lake is the discontinued operation we're talking about or they're talking about.

**Mr. Hillson:** — Okay. And what do you say is the total of losses for the operations of Channel Lake in the trading losses?

**Mr. James:** — The grand total of all the trading losses?

**Mr. Hillson:** — Yes.

**Mr. James:** — It would be the 2.4 million in 1996 plus the 3.1 million to March 1997, and then whatever was the amount after that, which at the time and based on March 31 prices was estimated to be 2.5 million.

So if I've got my math right, that's around 8 million, I believe, in total; you know, spanning essentially three periods: '96, the period that the company was owned by SaskPower, and then the period subsequent to that which . . . Anyway.

**Mr. Munro:** — Which effectively adjusted the purchase price.

**A Member:** — Pardon me?

**Mr. Munro:** — Which effectively adjusted the purchase price, because it was not realized that the mechanism of the purchase price reduced the purchase price for the unrealized gas trading losses.

**Mr. Hillson:** — Now, were you aware that March 31 was considered so significant by Saskatchewan Power management prior to this inquiry?

**Mr. James:** — Well, I think the answers to the questions previously about when we became aware and their objective is the extent of our knowledge. I mean this was not . . . this is one of very many things that we were dealing with in terms of an audit. And it was just a statement of fact that they were interested in selling and that we were informed, as Mr. Munro said, that they wanted to sell it by March 31.

**Mr. Munro:** — My perspective is that I never believed at the point in time when I sort of became aware that there was a target date of March 31 that that would affect the accounting or the disclosure with respect to financial statements of Channel Lake. And I believe that, in fact, it has not affected the disclosure or the accounting in respect of Channel Lake.

And I think the facts bear it out that we proceeded along to prepare final financial statements for Channel Lake. We've

prepared a report on internal controls that gets addressed to the Provincial Auditor. That has been tabled.

So it may well have been a more important date to SaskPower management, but I can't add any additional insight into why that was the case because I saw no way that that would sort of change what the disclosure might be.

**Mr. Hillson:** — And you are not consulted about whether reporting provisions would be altered by having it sold before March 31?

**Mr. Munro:** — No, and as I said . . . as we said in our testimony, clearly when we accepted the engagement to review the Channel Lake financial statements and provide our audited opinion on historical financial statements for purposes of the OPTUS prospectus, one of the reasons that I specifically asked SaskPower management about the Channel Lake financial statements is that I was not aware of whether they had ever tabled those financial statements in the Saskatchewan legislature.

And I was aware from reading the final purchase and sale agreement that there was a confidentiality clause within that purchase and sale agreement that said that the financial statements were supposed to remain confidential. And I'm also aware that when one files a prospectus those become matter of the public record, and so they became sort of effectively public financial statements at that point in time.

So I wanted to make sure that SaskPower management were aware that that was occurring. Because I wasn't aware whether they'd sort of done that through the normal tabling process.

**Mr. Hillson:** — And was there any discussions that you heard as to who was wanting the confidentiality clause? Was it the purchasers or was it SaskPower?

**Mr. Munro:** — I mean confidentiality agreements are almost a normal course of purchases of the sale of businesses, and our advice to our clients would be never let any potential purchaser look at your business without having a confidentiality version in place.

**Mr. Hillson:** — So it would be a standard, a normal expectation of any agreement of this sort?

**Mr. Munro:** — That's correct.

**Mr. Hillson:** — Now there is a discussion in the 1994 annual report, Saskatchewan Power, on the operation of Channel Lake. But after that, for the next two years, there is just one line about Channel Lake in the annual report.

**Mr. James:** — It would be helpful if you could perhaps indicate where it is in your . . . (inaudible) . . . please. Just to refresh my memory on what they said; I don't remember.

**Mr. Hillson:** — 1995.

**Mr. James:** — '95 or '94?

**Mr. Hillson:** — No, '94 does have some discussion of Channel

Lake's operations, but 1995, page 13.

**Mr. James:** — Yes, I see it.

**Mr. Hillson:** — I think the only reference is, development of Channel Lake Petroleum financial reporting and systems, the subsidiary is SaskPower's sole supplier of natural gas.

**Mr. James:** — Okay, yes.

**Mr. Hillson:** — I think that's the only reference receded to Channel Lake outside of saying that the financial statements are consolidated into Saskatchewan Power's financial statements.

**Mr. James:** — Yes.

**Mr. Hillson:** — And then 1996 again, I believe on page 21, I believe the only reference to Channel Lake is:

Drawing on marketing expertise, Channel Lake Petroleum continues to purchase natural gas at the lowest possible price for SaskPower's gas powered facilities.

**Mr. Munro:** — But I think I sort of . . . I know I'm breaking all the rules about answering questions before they're asked, but I never am very good at restraining myself.

**The Chair:** — That's why we have a Chair.

**Mr. Munro:** — That's right.

**The Chair:** — If you get too far out of line . . . (inaudible interjection) . . .

**Mr. Munro:** — Don't tell secrets.

**The Chair:** — That's why we have a Chair. If you get too far out of line . . . (inaudible interjection) . . . Mr. Gantfoer, I think you've scored a direct hit.

**Mr. Munro:** — That's right. There's without question in our mind that all of the financial reporting with respect to Channel Lake operations is entirely appropriate and is within accordance with generally accepted accounting principles, and it was all audited within accordance with generally accepted auditing standards.

In questions, I think you're sort of leading to a broader governance issue which I believe you've asked Deloitte & Touche to comment on. And I don't think that it would be really appropriate for us to sort of provide, where we have a basis to provide, whether there's sort of a whole bunch of additional disclosures on the various business units of SaskPower that would be appropriate in their financial statements, particularly given that the Channel Lake operations in and of itself, putting aside the sale process and the gas trading losses, wouldn't necessarily be material to the overall financial statements and operations of SaskPower.

**Mr. Hillson:** — What do you mean by that, Mr. Munro, that they're not material to the overall operations?

**Mr. James:** — Perhaps I can elaborate a bit because I've dealt

with SaskPower on disclosure of a number of issues over the years. And my perception of the reason they got into this in the first place was because they were running out of gas that was leftover inventory when SaskPower and SaskEnergy were divided. And I recall having discussions even . . . probably was in 1992, at the end of '92, the fact that their inventory levels were getting lower. They were burning the gas.

Gas is an integral fuel source for this corporation. If they didn't have access to gas your lights would go out in the winter at certain times. So it's crucial. It's not a luxury item for them. And when they explained to us that they were looking to buy these assets out of receivership, I mean there seemed to us to be a business case for that.

But I mean, I know you've had a lot of discussion on that, but just standing back and looking at this thing saying, so you're going to buy something for \$25 million and the objective of doing so is to help you manage one of your inputs, and one of your inputs that is subject to fluctuation in price.

I mean there seemed to be a reasonable business case. The amount of money they spent on it amounts to less than 1 per cent of the total assets of the company. I mean it's a very small amount. And I know . . . Don't get me wrong. I'm not trying to suggest this is an insignificant thing, but in relation to the total company, I mean they have to get gas like they have to get coal to burn, and it just seemed to us that their objective made sense. He went about it in a slightly different way than just going and buying gas at the market.

So I mean I wouldn't expect to see back in '93 or '94, '95, '96, frankly any disclosure even in the years you point out. I would certainly not have suggested to them that they should have said even what they said given that their sole objective was to acquire fuel. There aren't any stories in here either about coal contracts you know. I mean you wouldn't want to get into those; they're huge and very complicated.

But I mean it's just a way of getting something to burn to keep the lights on. I mean that's how I've always looked upon this until they got into the trading which, as we pointed out to them, is a different line of business than just securing fuel. It's something different and it has different risks attached to it. So I hope I'm answering your question.

**Mr. Hillson:** — I think what you're saying is you're not surprised that there would only be one line in the annual report. I think that's what you're saying.

**Mr. James:** — Correct. Sir, if this had been a \$250 million purchase instead of a \$25 million purchase, then I would definitely have expected to see more because it would have been much more significant compared to the total business.

**Mr. Munro:** — Effective 1998, companies are going to have to comply with the new *CICA Handbook* standard that deals with segmented disclosures where you have to provide, in addition to kind of the consolidated financial statement disclosures, disclosures in respect of business operations basically by business units.

But to be discloseable generally — and there's a whole host of

rules — but generally the assets and revenues have to be greater than 10 per cent of your assets or revenues. And my comment about . . . again, Mr. James said it perfectly. We're not sort of downplaying the significance of the Channel Lake operations, but in respect of the entire SaskPower financial statements they are not material.

**Mr. James:** — One other thing I might want to point out to you, if you look at the 1996 annual report, page 35, is the consolidated statement of income and reinvested earnings for 1996. And you will see there that there are two revenue lines, one that says . . . it says, electric operations, \$884 million; and gas operations, \$84 million. And if you look under expenses, you'll see fuel and purchase power, electric; and fuel and purchase power, gas. And you'll notice the numbers jump significantly.

Well the reason for that is because when we were talking to SaskPower about good disclosure in their financial statements we pointed out that because of the trading of gas, the volumes of revenues and the volume of expenses went up significantly and they were in fact gas operations. So we suggested to them that they should disclose those numbers.

Now there's no requirement to say that that Channel Lake *per se*, but it specifically says gas operations. People know this is an electric utility. To see gas operations jump from 12 million in revenue to 84 million in revenue, I mean, to me, tells me that something's happening in this organization that might be different than in the past.

But still they . . . And that is the sort of thing that Mr. Munro was just alluding to in terms of segmented information. To have simply shown total revenue of 968 million and implied it was all electricity would have been misleading. And we are dealing with an \$84 million item here.

So I mean it was disclosed at our suggestion because it's a different line of business than their electricity. So anyway, I hope that answers the question.

**Mr. Hillson:** — I think it does. I don't think you have been involved at all in SaskTel.

**Mr. James:** — No, I never have, other than as a customer — still.

**Mr. Hillson:** — And in there, the annual report just simply said that the corporation has decided to conclude its investment in NST, the cable company in Chicago, in that period. And you're saying that that sort of thing does not seem unusual to you, that you would have just one line in the annual report.

**Mr. James:** — I'd like to answer the question, but I'm sorry I'm not familiar with what's in SaskTel's annual report. I see it sort of every year, but it's circulated around. I read it for interest rather than scrutinizing it. So I'm sorry, I really can't answer that.

**Mr. Hillson:** — I'd like to turn to the management letter for 1995 . . . 1994, I'm sorry, CLP 7/6, and there are a number of recommendations you make there. Specifically the first one is concerning the management company at Channel Lake called

MVI (Management Ventures Inc.), and you make recommendations that there be changes to make sure that costs to Channel Lake are minimized.

Can you tell us if you are satisfied whether that was done?

**Mr. James:** — Could you please refer to the line? I'm sorry I . . . this is a lot of words in this one.

**Mr. Hillson:** — Yes, under recommendation no. 1.

**Mr. James:** — Okay.

**Mr. Munro:** — Sorry, Mr. Hillson, what was the question?

**Mr. Hillson:** — You make a recommendation that MVI services to Channel Lake be provided in such a manner . . . "which motivates MVI to minimize the cost to Channel Lake." Do you see that line there? Are you satisfied that was done?

**Mr. Munro:** — In our 1994 management letter we encouraged him to move to a form of contract with MVI that paid MVI a base fee plus some form of incentive to minimize costs. A final agreement with MVI to our knowledge was never concluded.

What they did do is that MVI provided services and Channel Lake, through Mr. Portigal, approved effectively all of the salaries because he sort of paid a base management fee and bought a basket of services from MVI. So MVI were responsible for providing a whole bunch of services and Channel Lake paid a management fee for doing that.

**Mr. Hillson:** — Right. But your recommendation is that we enter into an agreement with this management company which will encourage them to minimize costs to Channel Lake. Are you satisfied, was that done?

**Mr. Munro:** — I mean I'm not aware that there was ever a final agreement put in place with MVI.

**Mr. Hillson:** — So you're saying it wasn't done?

**Mr. Munro:** — No . . .

**Mr. Hillson:** — There is a recommendation here . . .

**Mr. Munro:** — There's a recommendation that they do that agreement. That particular agreement was not done. In respect of your question, were costs minimized with MVI, it's sort of a judgement question that would certainly be subject to separate analysis.

**Mr. Hillson:** — But it was your recommendation that they enter into an agreement with MVI that would hopefully minimize costs?

**Mr. Munro:** — Correct.

**Mr. Hillson:** — And no such agreement was ever finalized?

**Mr. Munro:** — That's correct.

**Mr. Hillson:** — Okay. Recommendation 2. You recommend

that there be a monthly reconciliation of accounts between Channel Lake and SaskPower. Can you tell me, was that recommendation acted upon?

**Mr. Munro:** — Yes that was.

**Mr. Hillson:** — That was complied with and that was done?

**Mr. Munro:** — Yes.

**Mr. Hillson:** — Okay. And recommendation three, that there be separate accounting streams within Channel Lake's books; a recommendation as to how Channel Lake do their accounting. Was that complied with?

**Mr. Munro:** — Yes.

**Mr. Hillson:** — And recommendation 4. Again a recommendation as to how information should be adjusted in the general ledger. Was that done?

**Mr. Munro:** — Yes.

**Mr. Hillson:** — Okay. And recommendation 5 is of course the recommendation regarding the gas trading activities. And I think again, it's common knowledge that no final policy was ever adopted on gas trading.

**Mr. Munro:** — That's correct.

**Mr. Hillson:** — Were you consulted over the next few years about a gas trading policy?

**Mr. Munro:** — I think as we referred to in our opening statement, that we did review two drafts of that gas trading policy during 1995.

**Mr. Hillson:** — And do you have any insight at all as to why it didn't go anywhere, didn't become finalized?

**Mr. Munro:** — I think I indicated to you that in respect of . . . or answering Mr. Gantefoer's question, that I am aware that as draft trading policies were developed it became apparent that, from a broader SaskPower perspective, they needed to direct their attentions to risk management activities. Now this moved it up to sort of the SaskPower level to deal with risk management issues. And I think that that . . . I believe that Mr. Portigal was waiting for input from a SaskPower perspective before he would say that he had final gas trading policies.

**Mr. James:** — SaskPower did strike, I believe they called it a risk management task force or something to that effect, dealing with the broad range of issues that an organization like this faces. Because there are a lot of everything from credit risk to operational risk whether . . . I mean there are all kinds of risks, some of which you can mitigate against. So this was one of the various areas of risk.

They started on this one, as we've said, earlier on than that; did come up with drafts. But we are not sure where that ended up in terms of the agenda of this task force. I know I can provide you no insight on that.

I mean we were encouraged by the fact that they were striking a risk management task force. You would expect any large organization to do that. I mean that's being proactive. This particular thing though, did not seem to perhaps receive the attention that perhaps it should have had. I have no other way of knowing other than speculating where it ended up.

**Mr. Munro:** — It's a matter of record as part of the SaskPower's internal auditor's report to SaskPower management on Channel Lake and our 1996 report to the Provincial Auditor, that there are draft policies in place but they weren't formalized. And it was difficult to determine whether they had been used by Channel Lake in terms of the conduct of their activities. And I can't add any further insight of why they didn't sort of get finalized.

**The Chair:** — Mr. Hillson, will you wrap up your questioning please.

**Mr. Hillson:** — You did bring up the issue of the need for a formal gas trading policy in subsequent management letters though?

**Mr. James:** — Okay, we mentioned it in . . . this is '94's, and as we indicated we did not issue a separate management letter in 1995.

We did discuss it though with . . . we knew what was going on. I mean it wasn't like a new item to raise with management because they knew that we'd been looking at drafts. I mean if your client says you've seen two drafts already, we're still working on it, you know you believe that they're still working on it. And in fact at the . . . been the spring of '96 audit committee meeting dealing with 1995 audit, I recall having a discussion again with the audit committee that, you know, this is in progress, we've seen drafts, and that was really the extent of it.

They were aware . . . And I should also point out when we had discussions with the audit committee on these reports they were concerned, they wanted to know more, they wanted to understand it.

So I mean they were certainly behaving in a way that I certainly would have expected an audit committee to behave. They were interested, asked questions, and wanted to know whether we thought they were going to be able to carry this out. And we said, yes, there's drafts and they're in progress. I don't know what else I could have said.

**Mr. Hillson:** — Okay, you say you did not issue a management letter in 1995?

**Mr. James:** — Correct.

**Mr. Hillson:** — Was one drafted?

**Mr. James:** — No.

**Mr. Hillson:** — Was there any particular reason why there was no 1995 management letter?

**Mr. James:** — Well as I said in the opening remarks, we were

dealing with the same people in management and we were dealing with the same people on the audit committee — audit and finance committee — as were there the previous year-end. When you go to the trouble of putting something in a letter and you discuss it with them, you know they start working on draft policies.

I mean we could have issued another letter repeating exactly the same point. I don't know if it would have proved anything; we're dealing with exactly the same people. Had there been a total change in management, clearly we might have taken a different approach. But I, at the time, saw no reason in reissuing the same letter.

**Mr. Hillson:** — Okay, so what you're . . .

**Mr. James:** — What I should say, though, had they done nothing, had there been no draft policies at all, I suspect our approach would have been different.

**Mr. Hillson:** — But if you had done the 1995 letter, you would have again said we need a contract with MVI and we need a gas-trading policy.

**Mr. James:** — Yes.

**Mr. Hillson:** — But you didn't do that because it would merely be a repetition of what you had said the preceding year.

**Mr. James:** — Precisely.

**Mr. Munro:** — And be clear for the record that in case of Channel Lake and again with SaskPower, because there's a sort of upward progression of reporting of results; that at our closing meeting of the 1995 audit of Channel Lake we met specifically with Mr. Portugal and talked specifically about their progress toward developing a final gas trading policy. And I know that you have a minute from Channel Lake records that speaks to the fact that conceptual draft policies had been approved by Channel Lake's board of directors.

And so we sort of . . . we brought the point up and I think it goes back to Mr. James' explanation to Mr. Gantfoer about the process of reporting verbally on sort of management letter points.

**Mr. Hillson:** — But in point of fact neither the MVI contract or the gas trading policy was ever formalized.

**Mr. Munro:** — Correct.

**Mr. Hillson:** — Thank you, Madam Chair.

**The Chair:** — Thank you, Mr. Hillson. I'll now recognize the New Democratic Party.

**Mr. Tchorzewski:** — Thank you, Madam Chair, and good morning, gentlemen. I just have one question on something which you referred to on page 15 and 16 mostly, and then I'll bow to my colleague, Mr. Kowalsky, who will then have other questions.

On pages 15 and 16 in your statement you speak to the gas

supply agreement. And on 16 you conclude that the agreement did not, in his view, suggest that the management fee in the agreement was significantly different from market rates. That led me to want to ask you about something which you may be able to comment on. And as you know, an appraisal firm prepared a report on the value of the Channel Lake assets, giving a variety of values depending on the discount rate that was used. SaskPower officials used the value attached to a 15 per cent discount rate.

I'm wondering if you can help the committee understand better about this discount rate, as to whether, in your view, the 15 per cent discount is an appropriate rate, or is it standard rate. I'm not sure whether you're in a position to comment, but if you can we certainly would appreciate that.

**Mr. Munro:** — Yes, but I want to be sort of fairly careful. In respect of the discount rates, I'll come back to in a minute because I think I can add comments.

You started off your comments or question speaking of the natural gas supply agreement, but I need to put that aside because that has nothing to do with what an appropriate discount rate might be in respect of oil and gas assets. I can tell you . . .

**Mr. Tchorzewski:** — The reason I asked the question because there has been discussion in the committee by witnesses and by questioning on the both sides about determination of the price having something to do with the gas purchase agreement, discount rates, and that kind of thing. So that's why I tied the two together. But I understand what you're saying.

**Mr. Munro:** — Okay, so putting aside — and appreciating why you did that — putting aside sort of the natural gas supply agreement for a moment. I have a significant base of oil and gas clients and I know when they buy and sell oil and gas properties, they would look to reservoir evaluations from firms like Gilbert Laustsen, and that as a starting point, they would have very similar information to what Gilbert Laustsen prepared and which I know the committee has seen.

And as a starting point many of my clients would use a discount rate around 15 per cent — as a starting point. Then the ultimate purchase price to be paid is dependent on a whole variety of factors I think which the representative from Gilbert Laustsen did a fairly articulate job of explaining why you would pick a different number than at 15 per cent.

And it really is motivation of the purchaser — your own particular perspective of where you think natural gas or oil prices are going, development potential for the properties. But as a reasonable starting point, I think that the 15 per cent number was a relevant number to be used.

And I believe that in Mr. Stewart's proposal letter where he did talk about a price and that his starting price was reflective of that 15 per cent. Now the difference is, is that Mr. Stewart built his proposal letter off a draft reserve report and I think there's been discussions earlier that there was an . . . (inaudible) . . . because one of the wells had gone to water.

So I hope that answers your question. I think it's a starting

point. I am aware of parties that would pay more money — that is except a lower discount — and I think that the Gilbert Laustsen officials said that there's lots of royalty trusts who seem to be paying that 12 per cent rate.

That's because basically what they're buying is a cash-flow stream and you're assuming a reserve risk for a cash-flow stream. And you're flowing that cash flow out to the holders of the royalty trust units. And royalty trusts were appealing because investors buy royalty trust units to get somewhat higher than a GIC (guaranteed investment certificate) rate.

But that 12 per cent rate wouldn't reward most of my oil and gas clients sufficiently to take on exploration and production risk. So they wouldn't pay a higher price or accept a lower discount rate.

**Mr. Kowalsky:** — Thank you very much, Madam Chair. Mr. Munro and Mr. James, it's my understanding that Ernst & Young were auditors for SaskPower prior to the time Dynex assets were acquired by Channel Lake Petroleum. Is that accurate?

**Mr. James:** — That's correct.

**Mr. Kowalsky:** — Did you do the audit work for SaskPower and its subsidiary when it was called Many Islands Pipe Lines Ltd.?

**Mr. James:** — Well, yes. Oh, you're stretching my memory. The first year I was ever involved was year ended December 31, 1987, and at which time SaskPower included what is now SaskEnergy — it was a gas and an electric business. And I do recall there being quite a small company called Many Islands Pipe Lines.

If you ask me anything much more specific than that, I'd have to go back to where our files from 10, 11 years ago I'm afraid. I do remember it; I don't remember any particular big issues or big dollars or anything flowing through it. I don't think it was particularly active.

**Mr. Kowalsky:** — Well do you recall that when it was determined that SaskPower would acquire gas properties and reserves through its subsidiary — be it Many Islands or Channel Lake — did you provide advice on how the subsidiary might be best structured?

**Mr. James:** — Not at all.

**Mr. Kowalsky:** — Did you provide advice from time to time on how the governance structure might be best managed? — the governance structure of this new company, Channel Lake?

**Mr. James:** — No. Well other than the comments made in the . . .

**Mr. Munro:** — We had a number of . . . If you go back to our management letters, most of them talked about establishing systems and procedures, and I would sort of call it sort of a very base level of governance.

**Mr. Kowalsky:** — But you didn't do anything prior to the

purchase of these assets.

**Mr. James:** — No definitely not.

**Mr. Kowalsky:** — Or in the planning for the purchase of the assets.

**Mr. James:** — No in fact when we first found out that they were going to buy them, I mean, they were in the process of doing it. I mean it wasn't something that they sort of came to us and said, we are considering doing this, would you give us some advice. There was none of that discussion at that time.

**Mr. Kowalsky:** — Thank you. I want to turn now to the reporting process. We've done some of this but just for clarification would . . . I would like you to sort of describe what your normal practice would be in presenting your annual report to SaskPower and to the Channel Lake board. What process would you go through? You mentioned that you go through a series of two meetings, I believe.

**Mr. James:** — Yes, okay. The first meeting with the audit and finance committee of the board. And this is . . . I have to say upfront, this is a fairly typical process in a lot of audit clients. This is not a particularly unusual situation in terms of auditors interacting with the board.

One normally would meet with management at the planning stage of the audit to understand what's gone on in the company during the . . . well almost a year. Typically you would do your planning in August or September or October, somewhere in that time frame for the year under audit. You would typically take a look through some of their internal financial statements, their internal packages, and a company like SaskPower produces these monthly.

So there's material there and you look through it and try to identify potential issues. You ask management, you say: what have you been doing, what's new and different, what controls might have you changed, what new computer systems have you put in place?

So you try and get the lay of the land and then you're trying to get an understanding of how that might impact your audit work.

Then you come up with a draft audit plan and you run it by management. You let them look at it and see if that seems to make sense from their point of view. It wouldn't make sense to go and audit something that really hadn't been done or perhaps we misunderstood it from the discussion. So they see it in draft, we finalize it, and then we meet with the audit committee.

And the piece I'm sorry I left out of that process is the Provincial Auditor's people also review our planning work. They look at the document. They also share with us their planning document and provide us with an opportunity to make comments on that. All right.

So then the Provincial Auditor and ourselves and management go to an audit committee meeting where in accordance with the roles, responsibilities, and duties of auditors, the task force recommendations, we take the lead in that discussion presenting our audit plan document to the audit committee and answer

their questions.

And then the Provincial Auditor or his representative will make comments about their letter, and any comments they wish to make on ours. All right, but typically there aren't a . . . it's not a very long discussion usually, maybe 20 minutes.

And then we do our audit work. And we show up — usually in SaskPower's case it's some time in February or in some years it could be early March depending on circumstances and people's timetables and so on. And at that meeting, management, most years, and there's variations each year depending on the request of the audit committee and so on, but typically what would happen is that management would present, if they haven't already, the financial statements of the company which they have prepared. We would sit there and observe that and . . . typically and add comments as we saw fit, and clearly are looking out for comments that management might make that are inconsistent with their comments to us in the course of the work.

So it's, I mean you could call it . . . it's a presentation and then a sort of round table discussion if you will, amongst the audit committee, management, and the auditors, and the Provincial Auditor's people as well. And that's strictly dealing with the financial statements — consolidated financial statements. That is not dealing with the rest of the annual report. Okay. We are not there at the audit and finance committee discussing the draft annual report.

Then what typically happens at that closing meeting is there's an in camera session where management leave the room. Some years the Provincial Auditor has stayed; some years the Provincial Auditor's left. I mean that's dependent on the year. And typically what happens is the audit and finance committee turns to us and says, is there anything that you think we need to know that you aren't comfortable reporting in front of management?

And we have that discussion, and typically there isn't anything that we're uncomfortable discussing in front of management. In fact my policy is always to make sure I've discussed everything with management no matter how difficult it might be because, you know, I just believe that's the right way to do it. And the Provincial Auditor, if they're in attendance, they'll make comments as they see fit.

And I alluded to the annual report. What will happen then is in a place like SaskPower where they have a communications department, they typically are in charge of the annual report process and they draft it, and management at various levels, various vice-presidents and so on, have a go at it.

At some point in the process we see a draft and we will read the entire document, pay particular attention to make sure the financial statements in there are the same ones that we audited and they spelled our name right and everything else. We look for inconsistencies and we usually make quite a number of suggestions in terms of this is confusing, or this doesn't make sense to me, or that's not consistent with what I understood. And ultimately they will publish it following that process. Does that answer the question?

**Mr. Kowalsky:** — Yes, that answers . . .

**Mr. James:** — Rather long answer I'm afraid, but . . .

**Mr. Kowalsky:** — It leads me to another one.

**Mr. James:** — Okay.

**Mr. Kowalsky:** — In your meetings, did you meet . . . did you annually discuss management with the audit and finance committee? Do you do it pretty well every year?

**Mr. James:** — Yes, I'm certain that in every single year that I have been involved in this company both as the . . . before I was a partner, I was an audit manager and would attend with a partner. So from the year 1987 to the most recent year end, every single one of those meetings, the audit and finance committee had an in camera session to ask if we had any comments about management or anything else.

**Mr. Kowalsky:** — What was your overall assessment of SaskPower management, particularly during the years '93 to '97? General overall assessment.

**Mr. James:** — In what respect are you asking that question? I mean that's a pretty broad question.

**Mr. Kowalsky:** — Well did you think that they were doing a particularly weak job or a particularly good job, or were you concerned about any aspect of the advice that you might have given them, whether it was followed or not followed. Does anything stand out in your mind?

**Mr. James:** — One thing that stands out, and I'm afraid I'm not going to touch a broad brush answer because it just is too much generalization and one would have to do a tremendous amount more work to be able to answer the broad brush question.

What I can say, particularly given the fact that most of our discussions would be related to things like financial statement disclosures and how to go about measuring things and that sort of thing, I always found the senior financial people in the company's finance group to be open to suggestions. I mean right down to the disclosure of Channel Lake discontinued operations. I mean they never had sort of an argument with someone that this is how it's got to be and they said, no we disagree. I mean I've never really encountered that.

They have people who typically will do research on an issue before they even present it to us. So typically they will provide us with a memo or whatever, saying this is the transaction we've done; this is our recommended accounting treatment. And we'll sit there and agree or disagree or debate it or whatever, or perhaps provide them with more information or precedents in other companies or whatever the situation might call for to be constructive.

But I mean not every client does that. A lot of clients just say, what's the answer. I mean they go out and they do the research. And I guess I'm always pleased when I see someone try to do that because it shows they're trying and they're thinking and they're doing the research. They don't always get it right, you

know. But that's why they're coming and asking us the question.

And we have not had sort of arguments or heated discussions about accounting disclosures. They're typically quite professional in terms of the way in which they have responded. And I'd have to say that would apply to the previous chief financial officer and controller. And I mean I've never encountered . . . we don't agree on absolutely everything all the time but it's constructive.

**Mr. Kowalsky:** — Well this impression that you would have had of SaskPower, then it would be communicated to the audit and finance committee. Do you know whether or not it . . . or would you have communicated it to the SaskPower board as a whole or would that be beyond your . . .

**Mr. James:** — No, since . . . I can't remember the year but I have not had occasion to meet with the full board of SaskPower in quite a number of years. And that's again a fairly typical process. Typically you would deal with the audit and finance committee which is a subcommittee of the board of directors. And typically one would go to a full board meeting if there was a major transaction or something like that that they wanted to hear our views on.

The last time I remember going to a full board meeting was when SaskEnergy and SaskPower were split. And I do recall attending a meeting — I believe I was the audit manager at that time — to talk about some of the issues and the fact that we qualified our financial statements in the year that they did it, or our report I should say.

**Mr. Kowalsky:** — So from the SaskPower board perspective, you would have no reason to believe that they would think that you would not be supportive or satisfied with SaskPower's management and their processes.

**Mr. James:** — Well I've never given them a *carte blanche*, everything was fine. I mean we always keep the discussion factual. Where we've had management letter points like that, we've simply said in the meeting that I really have nothing else to add on the point. We've had an open discussion with management in the room; I don't have something else to add. So typically those in camera discussions are not very long.

I mean, as I say, it's a very good mechanism to have a standard in camera meeting with one's auditor every time so that people aren't . . . you know, bells don't go off when suddenly one is held and people wonder what the problem is. And it's very good for the auditor to have that opportunity also.

But no, there's nothing that I've raised with them that is other than factual and is other than what's been reported on our letters already.

**Mr. Kowalsky:** — Thank you. I want to just deal now with a reference to the Deloitte & Touche report. In their conclusions, Deloitte & Touche report that managing boards such as existed at Channel Lake Petroleum, where SaskPower management were the board members, they indicated that this was not unusual in both public and the private sector. Would you agree with that?

**Mr. James:** — I would agree with that. I should also point out that that's the reason why our management letter is addressed to SaskPower's board . . . or I mean, sorry, SaskPower's management copied to SaskPower's audit and finance committee, because the board of directors of Channel Lake was management. So we wanted to elevate the reporting to the governance level of the holding corporation.

**Mr. Kowalsky:** — Is that practice beginning to be less and less prevalent in board structures today or is staying constant?

**Mr. James:** — Which practice?

**Mr. Kowalsky:** — The practice of using managing boards.

**Mr. James:** — I can't give you a generalized answer on that. It would depend on the nature of the company, the size of the company in relation to the parent, and I haven't done a sort of study to see if that's a trend or not in subsidiary companies.

**Mr. Munro:** — I can tell you I have responsibility for somewhat more than 20 public companies and I'm not aware of any where they would have 100 per cent owned subsidiary that they would ask one of their independent board members to sit on the board of that subsidiary. Because in almost all cases they would view the subsidiary as basically a business unit that should flow up in the normal reporting process to the full board of directors.

And in fact that's by and large how we approached the audit of Channel Lake. We basically looked at Channel Lake like a management unit and it had sort of separate management for that business unit. But we always ensure that all of that matters went directly up to, firstly, senior management at SaskPower.

Now that was easy often, because the three senior management members of SaskPower sat on the Channel Lake board. And secondly, to the full SaskPower audit and finance committee who then are discharged with the responsibility of reporting matters of significance to their board.

**Mr. Kowalsky:** — Was the management board structure at Channel Lake something that Ernst & Young commented on in their annual financial statement?

**Mr. Munro:** — No.

**Mr. Kowalsky:** — Was it your assessment over the years that Channel Lake management and the Channel Lake board failed to fully and adequately inform the parent, SaskPower?

**Mr. Munro:** — I guess my own perspective, for the record, is that Channel Lake's board and Channel Lake management I sort of tie fairly closely together because I believed that the . . .

**Mr. Kowalsky:** — You mean Channel Lake's board and SaskPower's management?

**Mr. Munro:** — Well, but I look at Channel Lake's management as being inclusive of the board members, from the perspective that they were also SaskPower board members. And my earlier comments were that they were sort of a business unit that ties together.

**Mr. Kowalsky:** — Well in the case of Mr. Portigal, who was not on SaskPower board or wasn't really part of SaskPower, was it your assessment that he would have failed to fully and adequately inform SaskPower?

**Mr. James:** — I don't know if I have any basis for . . . other than reading testimony, I have no really way of assessing that, I don't think. How about you?

**Mr. Munro:** — I mean I had no . . . I mean, I think that's the exact purpose of the hearings, to make a determination of whether he met those objectives. Those are much broader than what we as auditors, in auditing the financial statements, could ever sort of single-handedly turn our attention to in any event.

**Mr. Kowalsky:** — So it really wasn't part of your responsibility?

**Mr. Munro:** — Correct.

**Mr. Kowalsky:** — Did you have any reason to believe that SaskPower management was overly concerned with public perception as opposed to a commitment to good governance and management practices?

**Mr. James:** — Could you repeat that question?

**Mr. Kowalsky:** — Yes. Did you have any reason to believe that SaskPower management were overly concerned with public perception as opposed to commitment to good governance and management practices; how it would appear versus the substance?

**Mr. James:** — It's difficult to assess that I guess. I mean, the word overly requires a judgement. I mean I'd never really given it any thought.

Our focus has always been on discussing with management what's good disclosure in the financial statements. And we believe that the disclosure in the financial statements over the last few years has been reasonably good disclosure.

And as I said before, when we've suggested that something be disclosed, added, written a slightly different way in the notes, we haven't encountered a sort of stonewalling or objection. I mean typically, they're quite interested to know what our views are and most of the time will accept them.

So I mean I don't think that's indicative of someone who's, you know, afraid of public perception but I'm afraid we've never . . . I don't really know how to answer the question in its totality, I'm afraid.

**Mr. Kowalsky:** — I think you've answered it. Thank you very much.

**The Chair:** — Thank you, Mr. Kowalsky. I have an indication from Mr. Thomson he has questions.

**Mr. Thomson:** — Thank you, Madam Chair. I only have two quick questions really. Deloitte & Touche reported that the Channel Lake sale process was pursued with a sense of urgency. I guess I'm interested in whether your assessment that

SaskPower acted too urgently in the sale of Channel Lake and as a result made mistakes.

**Mr. James:** — Too urgently compared to what I'm afraid?

Again that requires a significant judgement call and I think you can see in Mr. Stewart's letter . . . I mean, he indicated their options.

**Mr. Thomson:** — I guess the question I'm asking is: too urgently in order to perform the necessary, fulfil the necessary responsibilities to make sure everything's looked after?

**Mr. Munro:** — Sure, I mean I really believe that that's ultimately the question that you're going to have to answer as a committee. Laying, sort of, all sorts of facts in front of you and . . . I mean whether the . . . if you determine that there were mistakes made, that's the determination you have to make; whether they were a result of trying to complete the sale in a 6-week period or 8-week period or some other factors I don't know.

**Mr. Thomson:** — You don't want to offer any advice on that?

**Mr. Munro:** — No.

**The Chair:** — The job of the committee.

**Mr. Thomson:** — Just trying to shorten things up, Madam Chair.

The only other question I really have is in terms of the internal process within Channel Lake and SaskPower, did you have any concern about the number of board meetings in the way that . . . how often the board met to deal with these matters?

**Mr. James:** — With either company.

Our knowledge of board meetings and their frequency is derived from reading the company's minutes at the end of the year.

And I've always noticed that SaskPower's board and audit and finance committee and other committees of the board do meet on a regular basis. It's not an audit and finance committee that only meets once a year or twice a year just to meet with us. I mean I know they do deal with other issues. They deal with issues that the internal audit department raises. It's an active working committee.

So I've never had the feeling that they . . . And to be honest with you, I've never thought whether they should meet every month or every two months. I mean if they were not having regular meetings several times a year, then I would be concerned.

But as far as Channel Lake, the board of that company goes, I mean my view on that again is that I mean it was management people in effect running a business unit. I don't see that as a particular governance structure *per se*. I mean it's like running a business unit.

**Mr. Munro:** — It's a management issue as opposed to a board

governance issue as to how's the board going to discharge sort of the best responsibilities for the ultimate shareholder. In Channel Lake, it was really a management issue of what process do we want to manage this business unit.

**Mr. James:** — I mean the fact of the matter is I don't think they could have bought Channel Lake assets in SaskPower directly given the way the legislation's written. But they are allowed to own a subsidiary.

So I mean had that impediment not been there, perhaps — I mean I'm speculating — but they could have put this directly into SaskPower, perhaps. I mean would you then have the same issue arise? Potentially you could. It's not necessarily dependent upon the legal structure.

**Mr. Thomson:** — That's what I wanted to know. Thank you very much.

**The Chair:** — Thank you. Are there any other questions from the government side? No. Are there any questions from the Saskatchewan Party? Any further questions from the Liberal Party?

**Mr. Hillson:** — Just two quick ones, Madam Chair. Were you asked for an opinion as to how the company should be sold and as to whether there ought to be public tendering?

**Mr. James:** — No, we were not.

**Mr. Hillson:** — Okay. Now there is an internal memorandum you're probably aware of as to whether or not Channel Lake could be removed from the books of SaskPower as of December 31, 1996.

**Mr. James:** — Be removed from the books as of December, yes. Okay.

**Mr. Hillson:** — You're aware of that memorandum?

**Mr. James:** — I'm aware of it from this testimony.

**Mr. Hillson:** — Yes. Were you consulted about that in any way?

**Mr. James:** — Not by memo *per se*. We were consulted on the accounting for the transaction. And as I indicated in the opening comments, there were some very brief initial discussions held in, I believe it was, in March '97 dealing with sort of hypothetical numbers as to how you would account for the gain or loss on the sale of a company.

I mean SaskPower doesn't do this very often. So I mean their accounting person I was meeting with . . . wasn't sort of thing they did all of the time. So they sat down and said, what are the mechanics. And we sort of did it on a piece of paper using round hundred dollar examples, and I said this is how you think about it all right.

And we didn't have another discussion on it until, specifically the accounting I believe, until January 1998. And a comment was made to me at a meeting about this accounting, that this agreement was effective January 1, 1997. And I said, well,

when did it close. Well it closed, I believe it was, June 2 — have I got that right, June 1, June 2? — June 1, and I said well in that period of time from January 1 to June 1 who had all the benefits and risks of ownership of this entity.

In other words if there was a catastrophe in Channel Lake, a big fire or a big problem, say in March, who was responsible for it. Well SaskPower would have been responsible for it obviously. I mean you wouldn't find the Direct Energy signing the agreement to buy something that was a catastrophe.

So as far as I was concerned, the January date was completely irrelevant. I mean every agreement has an effective date. That's just where you anchor your calculations all right. As far as I was concerned, they owned that company up until closing. And that's what drove the accounting.

And I said to them in that meeting in January: go and look in the *CICA Handbook*, section 3475, and it will tell you how to account for discontinued operation. Forget January 1; I don't care about January 1. And they understood that; there was no argument. They went away, looked at it, came up with the disclosure you see in these financial statements.

**Mr. Hillson:** — But do you have any idea why the question would have arisen as to whether we could remove it from the books as of December 31, 1996? Would you have any idea where that question came?

**Mr. James:** — No, I'm afraid I don't. I'd be absolutely having to speculate and I have no . . .

**Mr. Hillson:** — Nothing further, thank you, Madam Chair.

**The Chair:** — Thank you. Mr. Munro you're indicating you wish to . . .

**Mr. Munro:** — One comment. Our counsel points out that earlier this morning that I was in error in reference to a specific date, and I think I was referring to the Channel Lake-Direct Energy purchase and sale agreement, used a date of May 2. And the date obviously is April 2. So just for the record if I can place that in front of you.

**The Chair:** — Thank you. I'm going to test the parties again. Are there any further questions of the representatives for Ernst Young? Gentlemen, do you wish to make a closing statement at this time?

**Mr. James:** — Not at this time. Nothing further to say other than to thank you for your courtesy and wish you well in your task.

**The Chair:** — Thank you very much. You are now both excused, and Mr. Munro, you certainly can book a tour through the legislature.

I would like, before we break, I would like to know if any committee members have procedural matters. I do have one. Committee members will realize, it should come as no shock to anyone that things seem to be wrapping up in the legislature; and in order for us to be able to table our report, have it printed and distributed, I've consulted with the Clerk and we will

require an enabling motion so that we can table it intersessionally.

And I have . . . Ms. Woods and I have drafted a motion that I would propose to present to the legislature this afternoon. And I would ask Mr. Trew at this point to read it into the record.

**Mr. Trew:** — Thank you, Madam Chairperson. I move:

That the Standing Committee on Crown Corporations recommend to the Assembly that this committee upon completion of its investigation into the acquisition, management and sale of Channel Lake Petroleum Ltd. by SaskPower, and the payments to Mr. John R. Messer when he ceased to serve as president of SaskPower, be authorized to table its report thereon intersessionally by submitting the same report to the Clerk of the Assembly, whereupon such report shall be deemed to be tabled;

And further that upon receipt of the report of the committee, the Clerk of the Assembly shall: (a) cause a copy of the report to be delivered to all members of the Legislative Assembly; (b) distribute the report publicly as directed by the Standing Committee on Crown Corporations; and (c) make the report available for public inspection during normal business hours in the Office of the Clerk.

I so move.

**The Chair:** — Thank you. The motion has been moved. Do I have any questions or comments on it? Okay, the question has been called. All those in favour of the motion please indicate. That is unanimous. Thank you very much.

The hour now being after the normal hour of adjournment, we stand adjourned until 9 a.m. tomorrow morning at which point we will receive testimony from the CIC (Crown Investments Corporation of Saskatchewan) officials, Mr. John Wright and Mr. Michael Shaw.

The committee adjourned at 12:05 p.m.