

From: lanceclarke@lowerchurchillproject.ca
Sent: Thursday, July 18, 2013 12:36 AM
To: jason kean/nlhydro
Cc: paul harrington/nlhydro; gilbert bennett/nlhydro; brian crawley/nlhydro
Subject: Re: Draft IE Report to Ed / NL

Me too.

On 2013-07-16, at 8:02 PM, "Jason Kean"
<JasonKean@lowerchurchillproject.ca> wrote:

Paul,

I agree with your proposal.

Jason

Jason R. Kean, P. Eng., MBA, PMP

Deputy General Project Manager

PROJECT DELIVERY TEAM

Lower Churchill Project

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You owe it to yourself, and your family, to make it home safely every day. What have you done today so that nobody gets hurt?

Paul Harrington---07/16/2013 03:31:13 PM---Gentlemen I am intending to send the following response to Jim - I believe the IE's statements shoul

From: Paul Harrington/NLHydro

To: Gilbert Bennett/NLHydro@NLHydro, Lance Clarke/NLHydro@NLHydro, Jason Kean/NLHydro@NLHydro, Brian Crawley/NLHydro@NLHydro,

Date: 07/16/2013 03:31 PM

Subject: Re: Draft IE Report to Ed / NL

Gentlemen

I am intending to send the following response to Jim - I believe the IE's statements should be allowed to stand and may actually help to prepare the cost message. Before i send this note below I believe we should consider the recipients and the timing of this message - we need to start to lay down some markers as to where costs are going and having the IE state that the market conditions are driving them up passed what you could expect using contingency setting recommended practices may be step one.

here is what I have drafted - we will need to respond fairly promptly so feedback would be appreciated

Jim

I will review the full report but as you say that will take some days regarding the extract below.

The IE seems to be saying that at DG3 we did not have the major contract pricing in at that time so the estimate and contingency/escalation was based on "a multi-faceted

Project Risk Management Plan, and using AACEI's recommended practice, Nalcor has adopted a reasonable approach in the interim period."

The IE then states that other similar projects are carrying larger contingencies in the 12 to 18% range and indicates that is what we may expect to realize when we get the actual major contract pricing in hand. This reflects in the IE's opinion of the current market condition.

So I see a positive statement that at DG3 Nalcor took a reasonable approach based on recommended practices however that positive statement is balanced off by a cautionary note that the current market conditions are such that Nalcor can expect to receive actual contract prices for major contracts that will not conform to the contingency setting established by application of the AACEI recommended practice and a multi-faceted Project Risk management Plan.

Our experiences to date on PO/Contract prices from actual bids are that we are experiencing equipment/material costs which are on or around the DG3 estimate, however the Contractors are pricing the labour and sub contract costs much higher than our estimate based on their risk perception of carrying out work in NL using local contractors. The Vale project at Long Harbour and the poor productivity experienced there have driven civil costs up on LCP and this combined with a highly competitive overland transmission market has resulted in Contractors being in a dominant position- we continue to seek mitigations to these factors and are making some small gains but the overall effect may be line with the IE's predictions. So the statements should be allowed to stand and may assist in preparing for the project cost at Financial Close.

Regards Paul

Paul Harrington

Project Director

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James Meaney---07/16/2013 02:54:40 PM---Hi Folks I just wanted to give you a heads up.

From: James Meaney/NLHydro

To: Paul Harrington/NLHydro@NLHydro, Jason Kean/NLHydro@NLHydro, Lance Clarke/NLHydro@NLHydro,

Cc: Gilbert Bennett/NLHydro@NLHydro, Derrick Sturge/NLHydro@NLHydro, Auburn Warren/NLHydro

Date: 07/16/2013 02:54 PM

Subject: Draft IE Report to Ed / NL

Hi Folks

I just wanted to give you a heads up.

Both Ed and the Province have been asking about the latest draft of MWH's IE report. Ed is wondering what some of the "big issues" are and NL want a copy ASAP. You probably recall we had committed to provide this to NL as part of that LCP Governance & Controls session held a month or so ago. The consensus amongst Derrick, Auburn and I this morning was a copy of the report should go to Ed before the Province gets it and he should be made aware of any key

points. We also need to post to the data room for Canada today (given that they are the ultimate client of MWH).

I have scanned the July 12 draft which I forwarded on to Saturday morning (it's nearly 350 pages, so detailed review will take some more time). In my opinion it seems to be an improvement from the March 22 draft, but there's still a number of areas where they need to fill in gaps over the next few months as contracts become available for their review, etc.

The one area we I could see some potential sensitivities with Ed and Province is the level of Contingency in the DG3 estimate. Below is the latest commentary in this area:

Capital costs used in the Nalcor financial models include contingency as well as escalation, as shown in Table 9-1.

The level of accuracy supported by the amount of engineering performed at this stage of project

development should provide an adequate margin to mitigate the risk of uncertainty still present

in the absence of the larger contracts being awarded. At this point in our review, the IE is of the

opinion that allowances for contingencies should be greater than the figures provided by the Nalcor cost estimating consultants summarized in Table 9-1.

By arriving at the contingency levels used as input to the pro forma following a multi-faceted Project Risk Management Plan, and using AACEI's recommended practice, Nalcor has adopted a reasonable approach in the interim period. However, they have arrived at some figures that do not compare well to those used in other similar projects we have reviewed. The IE typically

sees contingency allowances in the range of 12 percent to 18 percent at this state of project development.

I have also included their commentary from the March 22 draft:

The level of project definition as evidenced by the amount of detailed engineering performed at

this project life-cycle stage provides an essential margin to mitigate uncertainties still present in

the absence of the larger contracts being awarded and executed. However, , the Independent

Engineer is of the opinion that contingency allowance for known or tactile risks should be

greater than the figures provided by Nalcor's cost estimating consultants. We maintain the

opinion that the underfunded tactile or scope contingency will place increasing pressure on the

utilization of the management reserve to mitigate project risks and other execution challenges.

This perception works against the common notion that the management reserve will not be

spent and will be front and center to deal with both known and unknown risks. The contingency

issues at odds will be reviewed with the objective of finding consensus among the professional

estimators. By arriving at the contingency level used as input to the pro forma following a multifaceted

Project Risk Management Plan, and using AACEI's recommended practice, NALCOR

has, adopted, in our opinion, an aggressive approach relative to risk management in the interim

period if the management reserve is not readily assessable. . We find that typically the scope

contingency for a Decision Gate 3 status would range between 10 percent to 15 percent of this state of project development. A separate management reserve allowance at 10% is also recommended for strategic or unknown unknown risk issues. Table 9-4 lists the current level of contingency provided by Nalcor in the financial model/pro forma.

They seem to have tempered their comments on "underfunded tactile or scope contingency" and "management reserve", but for some reason their comparison range has increased from 10-15% to 12-18%. I have a message in with Rey Hokenson to provide clarity on the basis of this change. That being said, I think view after Jason had a number of discussions with Jim Loucks following the March 22 draft was they have an overall view on the level of contingency and it's not going to change.

Putting this report in circulation with Ed and the Province may result in a renewed discussion on contingency. Just wanted to make sure you weren't blind sided by this. Feel free to give me a call with any questions or concerns.

Regards,

Jim

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James Meaney, CFA

General Manager Finance

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----- Forwarded by James Meaney/NLHydro on 07/16/2013 02:15 PM -----

From: James Meaney/NLHydro

To: "Jason Kean" <JasonKean@lowerchurchillproject.ca>, Auburn Warren/NLHydro, "Tom Garner" <thomas.f.garner@ca.pwc.com>, "Gordon Alexander" <GordonAlexander@nlh.nl.ca>, "Ed Over" <EdOver@lowerchurchillproject.ca>

Cc: "Derrick Sturge" <DSturge@nalcorenergy.com>, "Peter Madden" <PeterMadden@lowerchurchillproject.ca>, "Lance Clarke" <LanceClarke@lowerchurchillproject.ca>, "Paul Harrington" <PHarrington@lowerchurchillproject.ca>

Date: 07/13/2013 06:33 AM

Subject: Fw: DRAFT OF INDEPENDENT ENGINEER'S REPORT

Hi Folks

Attached is the latest draft of MWH's IE report. We will need to post this to the Intralinks data room for Canada/Cassels review by Tuesday

Please review the sections where you have provided input and advise of any comments or further clarifications. You will see they have highlighted in yellow some outstanding questions (Peter, I believe some of these you, Jason and I worked through Friday).

As we did with the March 22 draft, we will provide these to MWH and copy Canada.

Regards,

Jim

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From: Blaise Mitsutama [Chiemi.B.Mitsutama@mwhglobal.com]

Sent: 07/12/2013 05:34 PM CST

To: James Meaney; Leigh Anne Sutton

Cc: Reynold Hokenson <Reynold.A.Hokenson@mwhglobal.com>; Peter Madden; "lanceclark@nalcenergy.com" <lanceclark@nalcenergy.com>; Nalcor Energy IE & O&M <sm-am-ca-IE-OM-Nalcor@us.mwhglobal.com>; Celeste Christensen <Celeste.J.Christensen@mwhglobal.com>; Tsushin Chen <Tsushin.Chen@mwhglobal.com>; Mary Edwards <Mary.Edwards@mwhglobal.com>; Nikolay Argirov <Nikolay.V.Argirov@mwhglobal.com>

Subject: LOWER CHURCHILL: DRAFT OF INDEPENDENT ENGINEER'S REPORT

James and Leigh Anne,

Attached please find the Draft Independent Engineer's Report for the Lower Churchill Project.

Regards,

Chiemi B. Mitsutama ("Blaise")

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deleted by James Meaney/NLHydro]