



Nalcor Energy Internal Audit

Ethics Line Report 27

Conflict of Interest and Procurement



File 18-37

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Objective

The objective of this engagement was to review a complaint received through Nalcor Energy's Ethics line in October 2018 regarding Labrador Island Transmission Link (LITL) and [REDACTED]

The review had two objectives:

1. Conflict of Interest
 - Does a conflict of interest exist and if so, was it addressed in accordance with the Nalcor Energy Business Conduct and Ethics Policy? The policy requires disclosure of actual or perceived conflicts followed by the requirement to immediately address the conflict.
2. Procurement
 - Were Nalcor Energy's procurement practices appropriately followed?

Complaint Summary

The complaint received via Nalcor Energy Ethics line states [REDACTED] [REDACTED] to negotiate the purchase of the [REDACTED] in early 2018. No one from the project team or supply chain was involved in the solicitation or negotiation of the [REDACTED] is not an employee of Nalcor Energy or the Lower Churchill Project, but is a subcontractor on the project. It was later found out that [REDACTED] There was no RFP process and the purchase was sole sourced"

Internal Audit Process

Based on the allegations received, Internal Audit collected and reviewed the contracts, communications, procurement documentation and other documentation as deemed appropriate, along with completing interviews.

Background

[REDACTED]

In April 2017, changes to the implementation strategy with General Electric (GE) were completed via amendments of contract CDO501 (GE). A phased approach was implemented to allow first power to be delivered. At that time, the goal was that Monopole (Pole 1) of the HVdc system would be delivered by the end of 2017 with full bi-pole (Pole 1 & 2) by the beginning of 2019. As part of the contract renegotiation, a second set of protection and control cabinets/cubicle were to be installed at Stafford, UK to allow the bi-pole testing to continue while focus was placed on the mono-pole delivery. These additional cubicles were at a cost of \$5m. [REDACTED]

[REDACTED]

In February 2018, Labrador Island Transmission Link (LITL) entered into a purchase agreement with [REDACTED]. The purchase specifications included:

Product	[REDACTED]
Product Purpose	<ol style="list-style-type: none"> 1. Establish a “Centre of Excellence” training center for training of operators and technical personnel on HVdc Systems 2. Allow trouble shooting, testing and commissioning during dynamic commissioning.
Cost	\$1.6 million Cdn
Funding	To be funded through transfer from LITL contingency.
Procurement process	Product sole sourced as product used by all “major manufacturers”, including current supplier and installer of HVdc assets (GE).

Summary of Facts

Conflict of Interest

The allegation suggested that a LITL contractor [REDACTED] was involved in the procurement of equipment through [REDACTED] company.

Relationship

[REDACTED]

Ownership

Internal Audit was unable to obtain definite evidence (i.e. legal documentation) to confirm that [REDACTED] [REDACTED] however, based on publicly available information and an interview with [REDACTED] however, the percentage of ownership is unknown. It appears that 3-4 other individuals are also owners of the company, therefore assuming equal ownership, [REDACTED] could hold 20-25% ownership. He is also publicly listed as the Co-Founder, President, Director and Owner. The role and percentage of ownership is relevant as a smaller ownership stake would reduce the conflict. With a sole sourced contract, the full level of financial due diligence is not required; therefore, the corporation’s ownership would not necessarily be disclosed during the procurement process.

Procurement involvement

[REDACTED] was involved in the procurement process for the contract that was awarded to his [REDACTED]. One of his roles was to document the sole source justification for the [REDACTED] also coordinated and/or attended meetings related to the [REDACTED]. He coordinated and attended a meeting between the [REDACTED] himself and another utility that uses the [REDACTED] (a company he had previously worked with). He also coordinated a meeting with [REDACTED] which he did not attend.

Conflict of Interest process

██████████ indicated that he did disclose the relationship to Nalcor Energy via the project management team, but was not entirely sure to whom. He suggested several individuals to whom he likely disclosed the relationship. One of those individuals indicated that he did not know at the time of the purchase, but heard through other means several months later. ██████████ indicated that he was uncertain if he disclosed it to ██████████. All other individuals listed are no longer on the project. No documentation of the disclosure was maintained. ██████████ indicated that he was not aware of the relationship.

Conflict of Interest Conclusion

██████████ did not approve the purchase and the procurement process was appropriately completed, however, he should have been removed from the procurement process entirely. This is a violation of Nalcor Energy's Business Conduct and Ethics policy, which requires immediate action to address actual or potential conflicts of interest.

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Procurement Process and Decision

Required Documentation

The allegation suggested that the proper procurement process was not followed. Internal Audit reviewed all procurement documentations to ensure completeness and appropriate approvals. For this type of purchase, with a cost of \$1.6m, various procurement documents were required. Below is a list of the required documents, along with who approved them.

Procurement / Project Control Document	Approvals
Requisition	<ul style="list-style-type: none"> • HVdc Area Manager • Deputy Project Manager – HVdc • Cost control • Component Project Manager • Commercial Lead – HVdc specialties (for Supply Chain Manager)
Purchaser Order	<ul style="list-style-type: none"> • Component Project Manager • Commercial Lead – HVdc specialties (for Supply Chain Manager)
Sole Source Justification Form	<ul style="list-style-type: none"> • HVdc Area Manager • Commercial Lead – HVdc specialties (for Supply Chain Manager) • VP, Transmission
Project Change Notice	<ul style="list-style-type: none"> • HVdc Area Manager • Deputy Project Manager – HVdc • Cost control • VP, Transmission • EVP, Power Supply

Based on the number and role of the individuals (area management, project management, project controls, supply chain and vice president and executive vice president) approving the procurement documentation, it is evident that the purchase was not completed independently by the [REDACTED] and [REDACTED]. Note: Due to the dollar value of the purchase, the EVP was not required to sign the procurement documents. The Project Change Notice was approved by the EVP as the spending was to be moved from project contingency.

Appropriateness of purchase

As a conflict of interest did exist with the involvement of [REDACTED] in the procurement process, Internal Audit reviewed the appropriateness of the purchase and the use of the particular supplier to assess if an inappropriate purchased was made. Below are the facts of how the purchase occurred:

1. [REDACTED] was identified prior to involvement of both the [REDACTED] [REDACTED]. In the original GE contractor (2014), GE was requested to quote an “optional” cost for an [REDACTED]. This was not to be part of the contract cost, however, if Nalcor Energy decided

- to use the [REDACTED] the cost would be agreed upon. GE quoted 1.181 million GBP (which was \$2.15 million Cdn at the time).
2. In March 2015, a dynamic performance study was completed using GE's (formerly Alstom's) [REDACTED] (i.e. Alstom/GE owned and used a [REDACTED] for testing). A dynamic performance study is described within the documentation as a small subset of a Factory Acceptance Test (FAT). This was highlighted to be testing for Bipole implementation. This is when the transmission line was intended to be commissioned with both poles at the same time.
 3. In February 2016, a decision was made by Nalcor not to exercise the contract option to purchase the [REDACTED]. Although Internal Audit was not able to validate, it was suggested that this decision was based on cost and quality. The version that GE would provide was lesser than what was available.
 4. In April 2017, due to delays with the testing on the project and control software, the GE contract was renegotiated (by the CEO and EVP) to allow for the transmission line to be brought in with two stages (monopole and bipole). With the monopole operational, dynamic commissioning and testing would be completed both in Stafford and Newfoundland.
 5. In early 2018, the decision was made to purchase the [REDACTED] directly from [REDACTED] [REDACTED] (instead of through GE) as a sole source purchase. Sole source justification was written by [REDACTED] at the request of the project area manager. The area manager indicated that he was not aware of the [REDACTED] relationship and as [REDACTED] [REDACTED] he would be the logical choice. The purchase price was approximately \$0.5 m less than quoted from the main contractor and a 10% transfer fee was also waived.
 6. The timing of this purchase was consistent with the late 2017/early 2018 risk and performance reporting, which highlighted the risks and impacts of protection and control testing. The decision to purchase was based on several factors:
 - a. The [REDACTED] was deemed necessary in early in 2018 due to the lack of experienced HVdc operators in the province. This was also to be used as a training tool. Discussion and plans were made in early 2018 to install this asset into a training college in Holyrood. This did not occur, and the asset is now planned to be installed in the Core Science building at Memorial University when the building is completed. In the interim, the asset will be partially used in Soldier's Pond starting in January/February 2019.
 - b. Assist in trouble shooting, testing and commissioning of the monopole and bipole systems during static and dynamic commissioning. (i.e. consistent with GE contract renegotiation in 2017).

One alternative vendor was available; however, it is clear that [REDACTED] in the primary provider both in Canada and Internationally. Sole sourcing was based on technical standardization, specifically as the original equipment manufacturer (OEM) is using the same product.

Conclusion

The objective of this investigation was to determine if a conflict of interest existed and if any conflict impacted the vendor selection in the procurement process.

Conflict of Interest

At the time of procurement, any relationship that may bias (or appear to bias) the vendor selection must be must be addressed to remove the conflict of interest. ██████████ should have been removed from the procurement process entirely due to a conflict of interest. Although he indicated that he did disclose the conflict, it was not properly documented or managed due to, what appears to be, miscommunication.

Procurement

The investigation has concluded that Nalcor Energy procurement processes were followed. Procurement process allowed sole sourcing and the appropriate approvals were obtained. Internal Audit is comfortable with the vendor chosen and believes the involvement of ██████████ did not impact the vendor choice. The timing of the purchase was intended to align with commissioning activities along with negotiations to be installed in an educational/training facility. Due to delays in both, the asset was stored temporarily and will be partially used in Soldier's Pond starting in January/February 2019.

Recommendation

Conflict of Interest

1. Remove ██████████ from any further activity related to ██████████
2. Consistent with prior conflict of interest audits and recommendations; disclosure, assessments decisions and potential action plans for real or perceived conflicts should be documented.

Procurement

1. No recommendations.