

Nalcor Energy Internal Audit – NOTE TO FILE RE: Procurement and Conflict of Interest Investigation –
[REDACTED]**Background**

Three anonymous complaints were received through Ethicsline (Nalcor Energy's Whistleblower Line) in late January 2018 regarding Lower Churchill Management Corporation (LCMC) and [REDACTED]. Nalcor Energy Chief Executive Officer requested that Internal Audit complete an investigation related to these allegations and present findings to the Nalcor Energy Audit Committee. This investigation focused on conflict of interest and procurement activities. This investigation was completed during January, February and March 2018 and closed in April 2018. Referenced as Investigation #1 within remainder of this document.

Several months later an anonymous letter was received by the Chief Executive Officer. This letter was titled "On-going Conflict of Interest Investigation related to [REDACTED]". The letter was copied to the Chair of the Nalcor Energy Board, Minister of Natural Resources (Government of Newfoundland) and the Muskrat Falls Inquiry Forensic audit team. This letter contained similar allegations to the anonymous complaints received in January 2018. The Chief Executive Officer requested that Internal Audit review this additional letter and complete any additional work required.

The conclusions from Investigation #1 report were:

Procurement - Power Supply awarded the contracts within policy. Sole sourcing justification was completed and approved at the appropriate level. Procurement documentation to manage the contracts had opportunities for improvement.

Conflict of Interest – In compliance with Nalcor Energy policy, both Power Supply management and [REDACTED] management disclosed [REDACTED] prior history with the project.

Internal Audit has made recommendations related to the procurement processes to increase consistency between contracts and demonstrate work scopes were appropriately pre-approved. Internal Audit has also made recommendations related to conflict of interest processes at a corporate level.

Process for second letter

Internal Audit compared the two sets of allegations to determine if additional investigation procedures were required. Internal Audit also took previous internal audit work into consideration when assessing allegations (e.g. audits in change management, contract award, payment certificate audits). Commentary on each section of the new letter is included below. Response should be read in conjunction with the Investigation #1 report (named "Ethics line #8, 9, 11). Internal Audit also had another relevant audit planned for the shortly after this letter was received. This audit (LCP Cost control) reviewed information on several scopes of work (including GE). Internal Audit left this investigation open until the audit was completed to ensure no scopes of work for [REDACTED] were included in GE costs. No concerns were noted.

Conclusion

The information provided within this letter was consistent with the Investigation #1 and Internal Audit will use this document as support for the first report/investigation file. No additional report will be issued.

Ref #	Information from Letter	Internal Audit Comment
A	<p>In reference to the ongoing conflict of interest investigation being conducted by the Audit Committee of Nalcor Energy's ("Nalcor") Board of Directors regarding [REDACTED] and its relationship to the Muskrat Falls Project, the list of items below are being brought forward to ensure they are incorporated into the investigation.</p> <p>In performing its audit, Nalcor's Audit Committee should seek to confirm whether:</p> <ul style="list-style-type: none"> • Nalcor's Code of Business Conduct has been fully adhered too, in particular as it relates to potential conflicts of interest; and • Nalcor's contracting and procurement processes have been fully adhered too, and that there is a well-documented basis for business decisions made, including those listed below. 	<p>Similar allegations are noted within this 2nd letter in that the focus was on conflict of interest and procurement.</p> <p><i>Investigation #1 was confidential; therefore, it is unclear how the complainant was aware of the "ongoing conflict of interest investigation".</i></p>
1.	<p>Circumstances under which [REDACTED] was formed and timing therein. In October 2016 [REDACTED] was incorporated, in the Province of Newfoundland and Labrador, by four individuals [REDACTED] each of whom are presently listed as directors of the entity (reference Attachment 1).</p>	<p>Consistent and addressed within Investigation #1.</p>
2.	<p>Circumstances under which directors of [REDACTED] were and have been engaged by Nalcor to provide services for the Muskrat Falls Project. At the time of the incorporation of [REDACTED] each of these four directors were engaged directly by Nalcor through separate agency firms. Each held a junior to mid-level management role in [REDACTED] of the Muskrat Falls Project as is shown in the attached organization chart (see Attachment 2). In this capacity, [REDACTED] were working on the supply and installation of the [REDACTED]. [REDACTED] Shortly following the formation of [REDACTED] in October 2016, Nalcor entered into a services contract with [REDACTED] for the provision of the services of [REDACTED]. The services provided by [REDACTED] were not bid by Nalcor, but sole-sourced.</p>	<p>Consistent and addressed within Investigation #1.</p> <p>[REDACTED] component of the project was highly successful under the management these individuals, therefore, progression to more senior roles is expected and normal.</p> <p>[REDACTED] wanted the individuals to continue as transmission link contractors due to their prior experience on the project and the fact that their scope of work was concluding. At that point, the individuals informed [REDACTED] that they had formed [REDACTED] and wished to continue. [REDACTED] contacted IA and procurement (manager, business services) to discuss the structure prior to signing the agreements. The contract / purchase order structure and payment controls were set up to eliminate potential conflict. The PO structure was set up so the individuals were providing service – not the company, [REDACTED]</p>
3.	<p>Circumstances under which the directors of [REDACTED] were promoted to senior roles within the Muskrat Falls Project. Shortly after the formation of [REDACTED] as a legal entity, each of the [REDACTED] were promoted to senior-level management positions within the newly formed Power Supply division of Nalcor, wherein each of the individuals</p>	<p>Consistent and addressed within Investigation #1.</p> <p>Signing authority consistent with roles.</p>

	<p>were given financial signing authority on behalf of Nalcor and its entities (see Attachment 3).</p>	
<p>4.</p>	<p>Circumstances under which and rationale for, the directors of [REDACTED] receiving significant compensation adjustments. On or about November 2016, Nalcor executed a commercial agreement with [REDACTED] through which the services of each of the four noted directors was to be provided. Under this new commercial arrangement, compensation rates paid by Nalcor for the services, of these individuals, increased significantly, with [REDACTED] reaping significant mark-ups and profits.</p>	<p>Consistent within Investigation #1.</p> <p>The [REDACTED] did receive additional compensation starting in November 2016 due to restructuring of the Lower Churchill Project into two management groups (Power Supply and Power Generation). Power Supply was responsible for the transmission component of the project, including the Labrador Island Link, Labrador Transmission Assets and the HVDC components. Power Generation was responsible for the Muskrat Falls generation station. [REDACTED]</p> <p>[REDACTED]</p> <p>Prior to this organizational change [REDACTED] [REDACTED] The individuals were planning to leave the LCP as their scopes of work were ending. The new incorporated company was obtaining additional work outside of Nalcor Energy. Due to the change in the management structure, they did not leave, but did not want to close [REDACTED] as the new positions were short term. This structure was perceived to be a concern as the [REDACTED] [REDACTED] reporting to him. The Executive Vice President, Power Supply requested that the [REDACTED] [REDACTED] inform Internal Audit of this structure to ensure appropriate controls were put in place. Several controls were put in place including separate purchase orders, invoice approval processes and timesheet approval. As part of purchase order structure, [REDACTED] would not be receiving mark ups or profits on each individual and the individuals would essentially be separate contractors.</p>
<p>5.</p>	<p>Circumstances and limitations under which directors of [REDACTED] were delegated financial authority for Nalcor, and confirmation of oversight to ensure no abuse of authority occurred. Having been delegated Nalcor financial signing authority by the Nalcor EVP Power Supply, [REDACTED] knowingly delegated a portion of this authority to each of [REDACTED] in order to fulfill Nalcor's business requirements. With this signing authority, each</p>	<p>When [REDACTED] was originally identified as the [REDACTED] [REDACTED] additional controls were put in place due to the reporting relationships between the rest of the [REDACTED] Mr. MacIsaac would approve billings instead of [REDACTED]</p>

	<p>of ██████████ had the authority to negotiate and execute contracts on-behalf of Nalcor, but in doing so, adhering to Nalcor's Code of Business Conduct and contracting and procurement business process.</p>	<p>In relation to delegation of financial authority, delegation is a normal process and other embedded contractors were also budget holders.</p>
<p>6.</p>	<p>Circumstances and controls under which directors of ██████████ made significant financial commitments on behalf of Nalcor. In their new roles within Power Supply, on behalf of Nalcor, ██████████ negotiated contract amending agreements (i.e. change orders) and other commercial agreements with General Electric and Valard Construction, with values in excess of \$200 million dollars. ██████████ recommended, and was signatory to, several of these amending agreements, as demonstrated in Attachments 4 and 5.</p>	<p>GE negotiations were completed by the CEO and EVP, Power Supply. This was confirmed with the CEO and EVP, Power Supply.</p> <p>██████████ and John MacIsaac signed the amendments, which is appropriate in their roles at EVP and ██████████</p>
<p>7.</p>	<p>Circumstances and rational under which directors of ██████████ ended the provision of full-time services to Nalcor. Despite having been promoted to senior roles, and receiving substantial compensation increases some twelve-months prior, with the transmission project yet not complete, in late 2017 ██████████ elected to conclude their full-time assignments on the Muskrat Falls Project in order to advance ██████████ other business interests, including securing other contracts with several contractors with whom they had financial authority to manage /oversee on behalf of Nalcor.</p>	<p>The separate ██████████ contracts (Nov 2016) were due for renewal in late 2017. At this point, the ██████████ individuals decided to leave the project as independent contractors.</p> <p>This was reviewed as part of investigation #1.</p>
<p>8.</p>	<p>Circumstances under which since concluding a prominent role of ██████████ with the Muskrat Falls Project, ██████████ has been able to secure contracts for ██████████ with several of Nalcor's other contractors with whom he negotiated and approved change orders on behalf of Nalcor. Despite its relative infancy, in its LinkedIn page (Attachment 6), ██████████ is currently promoting a list of clients that includes General Electric, Valard, Nexans. It begs the question of whether these client relationships were formed at the expense of Nalcor and the taxpayers of Newfoundland and Labrador (i.e. promissory conditions for settlement of change orders), when ██████████ held financial signing authority for Nalcor and executed substantial change orders to existing contracts. As ██████████ was in a position to recommend the cost forecast for the transmission project, as presented by yourself in June 2017, which did present opportunities to over-inflate cost forecasts, therein providing the ability to settle claims with these contractors at terms very favourable to the contractors.</p>	<p>The LinkedIn page lists contractors/companies in which the individuals had previous experience working with versus companies in which they had current contracts.</p> <p>Internal Audit has reviewed the change management and procurement process in previous audits and found the processes to be robust with significant management of change.</p> <p>The most significant claims for the project are related to Muskrat Falls site vs. transmission under ██████████ and team. The main claim related to GE. As per discussion with both Nalcor CEO and EVP, Power Supply, ██████████ and team provided support to these negotiations administratively. The CEO and EVP negotiated the contract amendment. In the previous investigation, a reference to ██████████ receiving a piece of work from GE (\$5m) was alleged. Documentation was obtained demonstrating that ██████████ communicated to GE that they could not complete any LCP work for them due to their prior involvement in the project.</p>
<p>9.</p>	<p>Circumstances under which a contract between ██████████ and Nalcor was negotiated by ██████████ In 2017 ██████████ approved a sole-sourcing negotiation strategy (i.e. no bidding), led the negotiation, and awarded a contract to ██████████ for provision of commissioning services for Nalcor. This scope of this contract included the provision of commissioning personnel by ██████████ to Nalcor for the Muskrat Falls Project. ██████████ principal for the services would be ██████████</p>	<p>This was covered in investigation #1.</p> <p>Internal Audit discussed this with several Nalcor senior employees to understand how the ██████████ / Nalcor contract was initiated. As ██████████ had</p>

		<p>previously completed a HVDC line and [REDACTED] specifically), were deemed to be the most experienced HVDC individuals. Nalcor requested a tour & lesson learned session from several utilities across the country who had completed similar HVDC work. This was part of the Nalcor and Transition to Operations were initiating this (not the project team). The services of [REDACTED] were agreed upon during these sessions (by the EVP, not the [REDACTED])</p>
<p>10.</p>	<p>Circumstances under which following the execution of a contract between Nalcor and [REDACTED] and the mobilization of significant personnel, [REDACTED] subsequently departed [REDACTED] and became a director of [REDACTED]. Not only did [REDACTED] become a director of [REDACTED] but many of his associates also ended their relationship with [REDACTED] shortly thereafter and became employees of [REDACTED]</p>	<p>This was covered in investigation #1.</p>
<p>11.</p>	<p>Circumstances and basis under which Nalcor assessed that there was no apparent conflict-of-interest between [REDACTED] and accepted [REDACTED] proposal to provide commissioning services to Nalcor for the Muskrat Falls Project. At present, a significant number of commissioning personnel are being provided to Nalcor through [REDACTED] with the number growing each day. There was no competitive bid for these services.</p>	<p>This was covered in investigation #1.</p>
<p>12.</p>	<p>Circumstances and controls under which [REDACTED] has now become one of the larger services contractors to the Muskrat Falls Project. Despite having been formed in October 2016, [REDACTED] purports to now already have ~ \$20 million in sole-sourced (i.e. not bid) service contracts with Nalcor to provide services for the Muskrat Falls Project: Other local contractors are indicating that they are not being providing opportunity to participate, rather all work is being sole-sourced to [REDACTED] absent any competitive bid process.</p>	<p>Covered in Investigation #1.</p>
<p>13.</p>	<p>Confirmation that the directors of [REDACTED] upheld Nalcor Energy's Code of Business Conduct and contracting and procurement business processes when providing services to the Muskrat Falls Project and holding financial signing authority for Nalcor.</p>	<p>Covered in investigation #1.</p>