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a nalcor energy company

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November 12, 2020

Board of Commissioners of Public Utilities
Prince Charles Building
120 Torbay Road, P.O. Box 21040
St. John's, NL A1A 5B2

Attention: Ms. Cheryl Blundon
Director of Corporate Services & Board Secretary

Dear Ms. Blundon:

Re: Efficiency and Effectiveness Plan – Fall 2020 Update

In September 2019, Newfoundland and Labrador Hydro ("Hydro") submitted, as part of its joint evidence with Nalcor Energy in the *Rate Mitigation Options and Impacts Review* proceeding, a framework for Hydro's Efficiency and Effectiveness Plan ("EEP")[1] to achieve at least $4.5 million of sustainable cost savings. As committed in Hydro's correspondence of June 30, 2020, an update would be provided in the fall of 2020 with cost savings targets identified.

Enclosed is Hydro's EEP update with operational cost savings targets totalling $9.0 million by 2024 relative to the 2019 Test Year. Hydro will reflect the identified savings targets, as well as provide an update on its EEP key deliverables, in its next general rate application.

Should you have any questions, please contact the undersigned.

Yours truly,

NEWFOUNDLAND AND LABRADOR HYDRO

SWalsh

Shirley A. Walsh
Senior Legal Counsel, Regulatory
SAW/sk

Encl.

ecc: **Board of Commissioners of Public Utilities**
Jacqui Glynn
Maureen P. Greene, Q.C.
Kim Simms
Rate Mitigation Review

[1] Included as Appendix 3 to the "Reference to the Board on Rate Mitigation Options and Impacts – Evidence of Nalcor Energy & Newfoundland and Labrador Hydro," Nalcor Energy, September 20, 2019.

Nalcor Energy
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Efficiency and Effectiveness Plan

Fall 2020 Update

November 12, 2020

A report to the Board of Commissioners of Public Utilities

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1.0 Introduction

In September 2019, Newfoundland and Labrador Hydro ("Hydro") submitted its framework,[1] the Efficiency and Effectiveness Plan ("EEP"), for a cost savings plan to the Board of Commissioners of Public Utilities ("Board"). An update on Hydro's EEP was filed with the Board on June 30, 2020 in which Hydro outlined the impacts of the COVID-19 pandemic on its progress and a commitment to provide a further update, including costs savings targets, in the fall of 2020.

The foundational planning work required to identify cost savings targets and key deliverables for each of Hydro's strategic areas of focus has been completed. This report outlines: (i) Hydro's forecast operational savings targets for the period 2020 –2024, (ii) key deliverables for each of the priority areas of work identified in the EEP, and (iii) the supports Hydro has implemented to facilitate the shift in business priorities necessary to evolve its cost management culture and realize productivity gains.

2.0 Forecast Operational Savings Targets

Hydro is committed to continued cost management particularly given the rate pressures being experienced in the current operating environment. The areas of priority identified in the EEP are a means by which Hydro is refocusing its business to achieve cost savings and productivity gains; it is fully expected that cost savings will be achieved throughout all areas of Hydro's business as work on this plan progresses. Hydro is focused on long-term, sustainable cost savings.

The Board noted in its final report on the *Rate Mitigation Options and Impacts Reference* proceeding[2] that Hydro's plan for cost reductions was not sufficiently ambitious. Hydro acknowledges the Board's feedback.

As outlined in Table 1, Hydro has set multi-year operating and maintenance savings targets in excess of the $4.5 million originally committed. These forecast savings, for the period 2020 –2024, are benchmarked against costs included in Hydro's 2019 Test Year.

[1] Included as Appendix 3 to the "Reference to the Board on Rate Mitigation Options and Impacts – Evidence of Nalcor Energy & Newfoundland and Labrador Hydro," Nalcor Energy, September 20, 2019.

[2] "Reference to the Board – Rate Mitigation Options and Impacts Muskrat Falls Project – Final Report," Board of Commissioners of Public Utilities, February 7, 2020.

Table 1: Forecast Operational Cost Savings Targets 2020–2024 ($ millions)

	2020	2021	2022	2023	2024
Cumulative					
Hydro	1.0	3.1	4.2	5.4	6.5
Exploits Assets[3]	0.6	0.6	1.5	2.0	2.5
Total Savings - Cumulative	**1.6**	**3.7**	**5.7**	**7.4**	**9.0**
Total Savings – Incremental Annual	**1.6**	**2.1**	**2.0**	**1.7**	**1.6**

Hydro intends to reflect the savings targets indicated in Table 1 in its operating and maintenance costs in future test years. The savings targets identified may not result in an absolute reduction in future test year costs. For example, the 2022 Test Year operating and maintenance costs may not be $5.7 million less than the 2019 Test Year due to other changes in the business that may offset some of these savings including prudent cost increases, inflation, and other uncontrollable cost changes.

3.0 Evolving Hydro’s Business

3.1 Efficiency and Effectiveness Plan Snapshot

Table 2 outlines the commitments identified in Hydro’s EEP framework, as well as the key deliverables since identified.

Table 2: Commitments and Key Deliverables

Area of Focus	Framework Commitment	Key Deliverables
Work Management and Execution	Develop and implement a multi-year plan to centralize Hydro’s planning and scheduling function.	• Revise reporting structure to reflect an Integrated Planning and Scheduling Group. • Update and develop planning and scheduling and outage planning procedures. • Implement improvements to asset management and maintenance data records. • Develop work execution productivity baseline measure(s). • Align work management processes with asset management standards.

[3] Savings associated with the Exploits Assets will not be reflected in Hydro’s annual financial results or test year operating costs until such time as the anticipated acquisition occurs. Upon acquisition, the savings targets will be reflected on a Hydro consolidated basis.

Area of Focus	Framework Commitment	Key Deliverables
Technology	Identify, plan, and implement technology solutions to achieve operational advancements.	• Complete technology assessment of existing operations. • Undertake jurisdictional scan of comparable utilities. • Develop multi-year plan for new technologies identified and propose associated implementation strategy.
Exploits Assets[4]	Develop and implement a multi-year efficiency review of the Exploits assets.[5]	• Complete resource analysis and integration plan for integration of non-regulated operations into regulated operations. • Review reliability and cost optimization of assets. • Identify technology requirements to optimize productivity gains. • Develop five-year capital strategy.[6]
Capital Planning[7]	Maintain a focused capital planning approach to balance capital investment with cost management and reliability.	• Review current asset monitoring, risk-based decision-making, reliability metrics and industry practices to further transition to condition-based assessments. • Review estimating methodologies to investigate opportunities to improve capital planning at the budget phase. • Review project planning activities to improve capital planning at the execution phase. • Complete an analysis and implement improvements regarding capital underspends and carryovers.
Contracting and Procurement	Explore new opportunities for joint and consolidated procurement opportunities	• Complete current state analysis of procurement activities to determine baseline data. • Update and, where appropriate, increase Long Term Supply Agreements and Master Standing Agreements. • Review Public Procurement Act to determine

[4] "Exploits Assets" refers to three hydraulic generation powerhouse facilities (Star Lake, Grand Falls, and Bishop's Falls), the direct infrastructure associated with them (penstocks, power canals, etc.), the controlled and uncontrolled water sheds providing generation water, transmission lines, roads, and other associated infrastructure.

[5] Full optimization of efficiencies identified will depend on the transfer of the Exploits Assets from the Government of Newfoundland and Labrador to Hydro as a portion of the productivity gains will be a reflection of realization of opportunities both within the Exploits operations and Hydro's regulated operations. Should the transfer of assets not occur, opportunities for cost management and efficiencies will be pursued where achievable.

[6] Current non-regulated approach reflects annual capital submissions with planned capital expenditures expected to align with available cash flow from the Power Purchase Agreement.

[7] The outcome of the ongoing review of the Capital Budget Guidelines may impact some of the planned activity for this area of focus.

Area of Focus	Framework Commitment	Key Deliverables
		considerations necessary for joint procurement with external entities. • Review contracts with largest suppliers to identify potential value add opportunities • Develop multi-year plan for potential joint procurement opportunities with affiliated and non-affiliated entities.

3.2 Strategic Areas of Focus – Progress Update

3.2.1 Work Management and Execution

Hydro has completed research into utility best practice with respect to work management to assist in its determination of productivity metrics. As improved planning and scheduling approaches are implemented, benefits are expected to be realized in the areas of work management, work execution productivity, optimization of overtime, and optimization of outages. These benefits will be realized through improved planning and scheduling of both operations and maintenance and capital work as well as improved labor resource planning and the coordination of work and associated outages. Work has been completed to inform an appropriate reporting structure for an integrated planning and scheduling group and the establishment of this function is scheduled to occur in 2021.

Work has commenced in developing select planning and scheduling procedures and performance metrics and work management metrics have been established for oversight and monitoring. Improvements in this process are expected to continue into 2021 and 2022.

3.2.2 Technology

Earlier in 2020, Hydro had awarded a contract for an operational technology assessment by a third-party consultant and internal consultation sessions were completed prior to the COVID-19 pandemic. Progress of this assessment has been impacted as resources required to input into this process have been heavily engaged with evolving 2020 work plans to adjust to COVID impacts; however, the consultant is now nearing completion of its assessment of Hydro's existing operational technology and jurisdictional scan of comparable utilities. The consultant's findings will inform development of a multi-year plan that identifies recommended technologies and an associated implementation strategy.

3.2.3 Exploits

Hydro is seeking opportunity to reduce costs in Exploits through attrition and staffing integration[8] within its operations over a multi-year period. All resource costs including travel related expenditures are being analyzed across its geographic asset base (i.e., Star Lake, Grand Falls, and Bishop's Falls).

Opportunities to integrate the use of technology to advance communication and optimize productivity at remote locations within the Exploits regions are being explored. This review is being completed through the operational technology assessment currently underway.

Hydro has an assessment of budgeting and forecasting of the Exploits operations underway and is completing an analysis of operating and maintenance costs for 2021 and 2022. The development of a multi-year staffing reduction and resource integration plan is expected to commence in 2021 with implementation on a phased basis between 2022 and 2024 to transition from the current operations to the future integrated and regulated corporate structure.

3.2.4 Capital Planning

Hydro is reviewing its estimating and preparation phases of its capital budget process to identify opportunities for efficiencies and cost savings. A root cause assessment on all potential carryover of work for 2019 and 2020 will provide the foundation for a continuous improvement plan aimed at enhancing the execution of Hydro's annual capital plan.

Hydro will continue to identify opportunities to reduce its capital investments by further transitioning from age based to condition-based investment. The long-term goal in this area is the development of a multi-year plan to further transition from aged based to condition based investment, where appropriate.

3.2.5 Contracting and Procurement

To date, an internal technological solution that can support improved data gathering, analytics, and procurement processes has been identified and is expected to be implemented late 2020/early 2021. This is the foundational component of the initiative that will enable the Supply Chain Management

[8] The magnitude of integration to be achieved is dependent on the transfer of ownership of the Exploits Assets from the Provincial Government to Hydro

group to better track current and future contracts, enable procurement planning, and the identification of opportunities to leverage joint procurement internally and externally.

While the process of implementing this new technology is being progressed, procurement analytics are being performed on available data. A review of joint procurement opportunities is being identified both internally and externally through daily business transactions. Hydro is continuing to improve data gathering to identify these savings based on historical baseline prices. This will serve as the benchmark for future decision making in the identification of opportunities in operational efficiencies and realizable cost savings.

Hydro's Supply Chain Management group has been engaging with the Public Procurement Agency on a regular basis to identify and assess joint procurement opportunities. This has resulted in Hydro now participating in the NL Public Procurement Agency's Master Standing Offer Agreements for select services (i.e., shredding services, toilet tissue, and paper towel). An additional joint procurement opportunity was identified with the federal government for office supplies and paper.

During 2020, Hydro and Nalcor achieved joint procurement on flight pass savings. It is estimated that there is an average of 30% savings on each flight booked.

Hydro and Newfoundland Power have held discussions on a joint procurement initiative for LED[9] street lighting. This initiative has been reviewed with the Government of Newfoundland and Labrador's Chief Procurement Officer to ensure compliance with legislative guidelines from procuring with a non-government entity. Collaboration is ongoing with all stakeholders to advance this initiative.

3.3 Supporting Hydro's Business

Through the EEP, Hydro is evolving its business to operate as efficiently and cost effectively as possible. Human resource management, change management, and communication plans are integral to Hydro's ability to effect the required changes with minimal disruption to the business. As Hydro seeks to reduce costs, unintended consequences of reduced safety performance or reliability performance must aim to be avoided.

[9] Light emitting diode ("LED").

As Hydro undertook its analysis of the EEP's key areas of focus to determine the potential for productivity gains and cost savings, it was decided that labour management and workforce planning is critical to the success of each of the other five areas of focus. As such, Hydro is no longer treating human resources management as an independent area of focus; rather, elements of labour management and organizational restructuring have been reflected in the planned activities for each of the remaining five areas of focus, as required, and broader labour forecasting and human resource management support is considered to be a core support function that is required to support the entire EEP and Hydro's organization in general.

3.3.1 Human Resource Management

Approximately 60% of Hydro's operating costs are related to labour. Hydro is using its human resources data to optimize opportunities for sustainable labour cost reductions. Reductions in full-time equivalents ("FTE") are expected to be achieved primarily through attrition with potential modification of existing organizational structures and service delivery models to be considered.

In addition to a current assessment of FTE reductions, Hydro is working to improve budgeting and forecasting models to ensure departmental units have improved visibility into their labour profiles. This will result in enhanced management reporting during the hiring process and result in greater accountability for FTE management and timely decision making throughout the year.

In 2020, Hydro completed an in-depth review of human resource data on existing and future known vacancies to inform future workforce requirements and opportunities for permanent FTE reductions. An approximate 20 FTEs have been identified for elimination through attrition (e.g., known leaves, retirements, resignations, etc.) with savings anticipated to be realized during the period 2021–2022.

Hydro also conducted a review of its current vacancy allowance target. The vacancy allowance of 55 FTEs used in the 2019 Test Year is consistent with that to be used for 2020 and 2021 and will increase to 57 FTEs in 2022. This increased vacancy allowance is an aggressive target when considered in light of the reduced work force (i.e., approximately 20 fewer FTEs). The sustainability of this current assessment and forecast of the vacancy allowance is subject to sensitivity and pressure pending outcomes from decisions on rate mitigation, collective bargaining negotiations, and staffing requirements for the Holyrood Thermal Generating Station plant life extension[10].

3.3.2 Change Management and Communications

Change management is an important component of Hydro's strategy in evolving its business. Critical to success is helping those who are impacted by change understand the reason(s) for change and associated outcomes anticipated as well as to be consulted early in the process to allow for integration of input. Change management training was completed in 2020 with a core group of people working on the Efficiency and Effectiveness Plan initiatives and necessary engagement activities are underway with various internal and external stakeholder groups.

Similar to the application of change management practices, frequent and clear communication is critical to the success of evolving Hydro's business. Communications activities are focused on ensuring employees understand the purpose of the changes, the impact on the organization, how they may occur, and the impact of the change on employees. Additionally, overarching communication to the organization surrounding Hydro's commitment to cost management and the priority areas of focus will continue.

4.0 Conclusion

Hydro is targeting operational cost savings totalling $9.0 million by 2024 relative to the 2019 Test Year. As Hydro's business evolves and a culture of efficiency and sustainable cost management is further developed, Hydro expects other opportunities for sustained cost savings will be identified and pursued. Hydro fully expects that as it adapts and evolves its business over the five-year period (2020–2024), its plan for cost savings and advancement of its work in the priority areas of focus will also evolve. Hydro continues to focus on long-term, sustainable cost savings and productivity gains; such change will take time to manifest within the organization. Hydro will reflect the savings targets identified, as well as provide an update on its EEP key deliverables, in its next general rate application.

[10] The current assessment reflects Hydro's current structure and does not contemplate any potential corporate evolution of Hydro or Nalcor and its affiliates.