LABRADOR TRANSMISSION CORPORATION
FINANCIAL STATEMENTS
December 31, 2014

DIRECTORS

EDMUND MARTIN
President and Chief Executive Officer

GILBERT BENNETT
Vice President

DERRICK STURGE
Vice President, Finance and Chief Financial Officer

PAUL HUMPHRIES
Vice President, System Operations and Planning

ANN MARIE HANN
President, Coal Association of Canada

CHRIS WOODFORD
Architect, Woodford, Sheppard Architecture

OFFICERS

EDMUND MARTIN
Chairperson
President and Chief Executive Officer

GILBERT BENNETT
Vice President, Lower Churchill Project

DERRICK STURGE
Vice President, Finance and Chief Financial Officer

PAUL HUMPHRIES
Vice President, System Operations and Planning

WAYNE CHAMBERLAIN
General Counsel and Corporate Secretary

PETER HICKMAN
Assistant Corporate Secretary

JAMES MEANEY
General Manager, Finance

AUBURN WARREN
General Manager, Commercial, Treasury and Risk

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Independent Auditor's Report

To the Directors of Labrador Transmission Corporation

We have audited the accompanying financial statements of Labrador Transmission Corporation which comprise the statement of financial position as at December 31, 2014 and the statements of comprehensive loss, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Labrador Transmission Corporation as at December 31, 2014 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Deloitte LLP

Chartered Professional Accountants
March 18, 2015

LABRADOR TRANSMISSION CORPORATION
STATEMENT OF FINANCIAL POSITION

As at December 31 (thousands of Canadian dollars)	Notes	**2014**	2013
ASSETS			
Current assets			
Restricted cash	5	**106,032**	69,978
Trade and other receivables	6	**12,717**	102
Prepayments		**404**	323
Total current assets		**119,153**	70,403
Non-current assets			
Property, plant and equipment	7	**321,281**	126,702
Long-term investments	8	**224,746**	396,717
Long-term prepayments		**1,081**	843
Total assets		**666,261**	594,665
LIABILITIES AND SHAREHOLDER'S EQUITY			
Current liabilities			
Trade and other payables	9	**62,910**	18,960
Non-current liabilities			
Long-term debt	10	**468,102**	468,107
Total liabilities		**531,012**	487,067
Shareholder's equity			
Share capital	11	**1**	1
Shareholder contributions	11	**135,537**	107,631
Deficit		**(289)**	(34)
Total shareholder's equity		**135,249**	107,598
Total liabilities and shareholder's equity		**666,261**	594,665

Commitments and contingencies (Note 16)

See accompanying notes

On behalf of the Board:

DIRECTOR

DIRECTOR

LABRADOR TRANSMISSION CORPORATION
STATEMENT OF COMPREHENSIVE LOSS

For the year ended December 31 (with comparatives for the one-month period ended December 31, 2013)(thousands of Canadian dollars)	Notes	**2014**	2013
Expenses			
Operating costs		**(255)**	(34)
Loss for the period, being the comprehensive loss for the period		**(255)**	(34)

See accompanying notes

LABRADOR TRANSMISSION CORPORATION
STATEMENT OF CHANGES IN EQUITY

For the year ended December 31 (with comparatives for the one-month period ended December 31)(thousands of Canadian dollars)	**Notes**	**Share Capital**	**Contributed Capital**	**Deficit**	**Total**
Balance at January 1, 2014		**1**	**107,631**	**(34)**	**107,598**
Total comprehensive loss for the period		**-**	**-**	**(255)**	**(255)**
Contributed capital	11	**-**	**27,906**	**-**	**27,906**
Balance at December 31, 2014		**1**	**135,537**	**(289)**	**135,249**
Balance at November 13, 2013		-	-	-	-
Total comprehensive loss for the period		-	-	(34)	(34)
Issuance of share capital	11	1	-	-	1
Contributed capital	11	-	107,631	-	107,631
Balance at December 31, 2013		1	107,631	(34)	107,598

See accompanying notes

LABRADOR TRANSMISSION CORPORATION
STATEMENT OF CASH FLOWS

For the year ended December 31 (with comparatives for the one-month period ended December 31, 2013) (thousands of Canadian dollars)	Notes	**2014**	2013
Cash provided from (used in)			
Operating activities			
Loss for the period		**(195)**	(34)
Adjusted for items not involving a cash flow:			
Accretion of long-term debt		**(5)**	-
Changes in non-cash working capital balances	17	**31,335**	17,582
Increase in prepayments		**(319)**	(1,166)
Net cash from operating activities		**30,816**	16,382
Investing activities			
Additions to property, plant and equipment	7	**(194,639)**	(17,795)
Decrease (increase) in investments	8	**171,971**	(396,717)
Net cash used in investing activities		**(22,668)**	(414,512)
Financing activities			
Issuance of long-term debt	10	**-**	468,107
Increase in restricted cash	5	**(36,054)**	(69,978)
Change in contributed capital	11	**27,906**	-
Issuance of share capital	11		1
Net cash (used in) provided from financing activities		**(8,148)**	398,130
Net change in cash and cash equivalents		**-**	-
Cash and cash equivalents, beginning of period		**-**	-
Cash and cash equivalents, end of period		**-**	-

Supplementary cash flow information (Note 17)

See accompanying notes

1. DESCRIPTION OF BUSINESS

Labrador Transmission Corporation (Labrador Transco or the Company) was incorporated on November 13, 2013 under the laws of Newfoundland and Labrador to design, construct, finance, operate and maintain the Labrador Transmission Assets (LTA), which includes two 900 megawatt rated transmission lines connecting the Muskrat Falls hydro-electric plant, the Churchill Falls (Labrador) Corporation hydro-electric facility, the Labrador-Island Link (LIL) and certain other portions of the transmission system in Labrador. The head office of Labrador Transco is located in St. John's, Newfoundland and Labrador.

Labrador Transco is a 100% owned subsidiary of Nalcor Energy (Nalcor).

Newfoundland and Labrador Hydro (Hydro), Muskrat Falls Corporation (Muskrat Falls), and Labrador Transco have entered into the Generator Interconnection Agreement (the GIA), which governs the development and operation of the LTA. Under the terms of the GIA, Labrador Transco will recover all costs associated with the LTA from Muskrat Falls, which in turn will recover all costs incurred under the GIA as part of a power purchase agreement (PPA) with Hydro.

2. SIGNIFICANT ACCOUNTING POLICIES

2.1 Statement of Compliance and Basis of Measurement

These annual financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB). Labrador Transco has adopted accounting policies which are based on the IFRS applicable as at December 31, 2014, and include individual IFRS, International Accounting Standards (IAS), and interpretations made by the IFRS Interpretations Committee (IFRIC) and the Standing Interpretations Committee (SIC).

These annual audited financial statements have been prepared on a historical cost basis. The annual audited financial statements are presented in Canadian dollars and all values rounded to the nearest thousand, except when otherwise noted.

These annual audited financial statements were approved by Labrador Transco's Board of Directors on March 6, 2015.

2.2 Basis of Consolidation

These financial statements include only the financial statements of Labrador Transco.

Labrador Transco includes the financial statements of investees (including structured entities) only when it has control as defined in IFRS 10 - Consolidated Financial Statements (IFRS 10). In accordance with IFRS 10, control is achieved when Labrador Transco:

- has power over the relevant activities of the investee;
- is exposed, or has rights, to variable returns from its involvement with the investee; and
- has the ability to use its power to affect those returns.

The Muskrat Falls/Labrador Transmission Assets Funding Trust (Funding Trust) was formed under the laws of the Province of Newfoundland and Labrador and the federal laws of Canada on November 4, 2013 for the purpose of issuing long-term debentures to the public, which are guaranteed by the Federal Government of Canada, and to on-loan the proceeds to Muskrat Falls and Labrador Transco. The funds will be used for the sole purpose of constructing the Muskrat Falls hydro-electric plant and the Labrador Transmission Assets as part of Phase One of the Lower Churchill Project.

Based on the criteria outlined in IFRS 10, Labrador Transco has determined that it does not have control of the Funding Trust and as such has not included the accounts of the Funding Trust in these financial statements.

2.3 Restricted Cash

Cash held in accounts administered by a Collateral Agent is classified as restricted cash.

2.4 Trade and Other Receivables

Trade and other receivables are classified as loans and receivables and are measured at amortized cost using the effective interest method.

2.5 Property, Plant and Equipment

Items of property, plant and equipment are recognized using the cost model and thus are recorded at cost less accumulated depreciation and accumulated impairment losses, if any. Cost includes materials, labour, contracted services, professional fees and borrowing costs capitalized in accordance with Labrador Transco's accounting policy outlined in Note 2.6. Costs capitalized with the related asset include all those costs directly attributable to bringing the asset into operation.

Property, plant and equipment are not depreciated until assets are substantially complete and ready for their intended use.

Amortization is calculated on a straight-line basis over the estimated useful lives of the assets as follows:

Project support assets	4 - 5 years

2.6 Borrowing Costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalization. All other borrowing costs are recognized in profit or loss in the period in which they were incurred.

2.7 Impairment of Non-Financial Assets

At the end of each reporting period, the Company reviews the carrying amounts of its non-financial assets to determine whether there is any indication that those assets may be impaired. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash generating unit (CGU) to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual CGUs, or otherwise they are allocated to the smallest group of CGUs for which a reasonable and consistent allocation basis can be identified.

The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted. If the recoverable amount of an asset (or CGU) is estimated to be less than its carrying amount, the carrying amount of the asset (or CGU) is reduced to its recoverable amount. An impairment loss is recognized immediately in profit or loss.

2.8 Provisions

A provision is a liability of uncertain timing or amount. A provision is recognized if the Company has a present legal obligation or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Provisions are not recognized for future operating losses. The provision is measured at the present value of the best estimate of the expenditures expected to be required to settle the obligation using a discount rate that reflects current market assessments of the time value of money and the risks specific to the liability. Provisions are re-measured at each statement of financial position date using the current discount rate.

2.9 Revenue and Expense Recognition

Revenue is recognized on an accrual basis as earned when recovery is probable and revenue can be reliably measured. Expenses are recorded as incurred and consist of organizational, operational and other expenses associated with the operation of the Company.

2.10 Net Finance Income and Expense

For all financial instruments measured at amortized cost, and interest bearing financial assets classified as available-for-sale (AFS), interest income or expense is recorded using the effective interest rate, which is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or liability.

2.11 Foreign Currencies

Transactions in currencies other than Labrador Transco's functional currency (foreign currencies) are recognized using the prior month end close rate. At the end of each reporting period, monetary items denominated in foreign currencies are translated at the rates of exchange in effect at the period end date. Foreign exchange gains and losses resulting from fluctuations associated with borrowing costs are capitalized.

2.12 Income Taxes

The Company is exempt from paying income taxes under Section 149(1) (d.2) of the Income Tax Act.

2.13 Financial Instruments

Financial assets and financial liabilities are recognized in the Statement of Financial Position when the Company becomes a party to the contractual provisions of the instrument and are initially measured at fair value. Subsequent measurement is based on classification. Financial instruments are classified into the following specified categories: financial assets 'at fair value through profit or loss (FVTPL)', 'AFS' financial assets, loans and receivables, 'held-to-maturity investments', financial liabilities 'at FVTPL', financial instruments used for hedging and other financial liabilities. The classification depends on the nature and purpose of the financial instruments and is determined at the time of initial recognition.

<u>Classification of Financial Instruments</u>

The Company has classified each of its financial instruments into the following categories: loans and receivables, held-to-maturity investments and other financial liabilities.

Restricted cash	Loans and receivables
Trade and other receivables	Loans and receivables
Investments	Held-to-maturity
Trade and other payables	Other financial liabilities
Long-term debt	Other financial liabilities

(i) Effective Interest Method

The effective interest method is a method of calculating the amortized cost of a financial instrument and allocating interest income or expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial instrument, or, where appropriate, a shorter period to the net carrying amount on initial recognition.

Income or expense is recognized on an effective interest basis for financial instruments other than those financial assets and liabilities classified at FVTPL.

Financial Assets

(ii) Financial Assets at FVTPL

Financial assets are classified as at FVTPL when the financial asset is either held for trading or it is designated as at FVTPL.

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling it in the near term; or

- on initial recognition it is part of a portfolio of identified financial instruments that the Company manages together and has a recent actual pattern of short-term profit-taking; or

- it is a derivative that is not designated and effective as a hedging instrument.

A financial asset other than a financial asset held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or

- the financial asset forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Company's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or

- it forms part of a contract containing one or more embedded derivatives and IAS 39 Financial Instruments: Recognition and Measurement permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial assets at FVTPL are stated at fair value, with any gains or losses arising on re-measurement recognized in profit or loss.

(iii) Loans and Receivables

Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as loans and receivables. Loans and receivables are measured at amortized cost using the effective interest method, less any impairment. Interest income is recognized by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

(iv) Held-to-Maturity Investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity dates that the Company has the positive intent and ability to hold to maturity are classified as held-to-maturity investments. Held-to-maturity investments are measured at amortized cost using the effective interest method less any impairment, with interest revenue recognized on an effective yield basis.

(v) AFS Financial Assets

AFS financial assets are non-derivative financial assets that are designated as available for sale or are not classified in any of the previous categories. Gains and losses arising from changes in fair value are recognized in other comprehensive income and accumulated in the fair value reserve with the exception of impairment losses, interest calculated using the effective interest method, and foreign exchange gains and losses on monetary assets, which are recognized in profit or loss. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously accumulated in the fair value reserve is reclassified to profit or loss.

<u>Financial Liabilities and Equity Instruments</u>

(vi) Classification as Debt or Equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

(vii) Financial Liabilities at FVTPL

A financial liability may be classified as FVTPL if the contracted liability contains one or more embedded derivative, and if the embedded derivative significantly modified the cash flows or if the embedded derivative is not closely related to the host liability.

(viii) Other Financial Liabilities

All financial liabilities are classified as other financial liabilities. Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs. Other financial liabilities are subsequently measured at amortized cost using the effective interest method, with interest expense recognized on an effective yield basis.

(ix) Derivative Instruments and Financial Instruments Used for Hedging

A derivative is a financial instrument or other contract whose value changes in response to a change in its underlying variable, requires little or no net investment and is settled at a future date. Derivatives are initially measured at fair value at the date the derivative contracts are entered into and are subsequently measured at their fair value at the end of each reporting period. The resulting gain or loss is recognized in profit or loss immediately unless the derivative is designated and effective as a hedging relationship.

2.14 Derecognition of Financial Instruments

The Company derecognizes a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Company neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, its retained interest in the asset and an associated liability for amounts it may have to pay is recognized. If the Company retains substantially all the risks and rewards of ownership of a transferred financial asset, it continues to recognize the financial asset and also recognizes a collateralized borrowing for the proceeds received. The Company derecognizes financial liabilities when, and only when, its obligations are discharged, cancelled or they expire.

2.15 Impairment of Financial Assets

Financial assets are assessed for indicators of impairment at the end of each reporting period. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been affected.

Evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organization.

For certain categories of financial assets, such as trade receivables, assets that are assessed not to be impaired individually are, in addition, assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Company's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period, as well as observable changes in national or local economic conditions that correlate with defaults on receivables.

For financial assets carried at amortized cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited to the allowance account. Changes in the carrying amount of the allowance account are recognized in profit or loss.

When an AFS financial asset is considered to be impaired, cumulative gains or losses previously recognized in other comprehensive income (loss) are reclassified to profit or loss in the period. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized.

2.16 Adoption and Amendments to IFRSs

In the current year, Labrador Transco has applied a number of amendments to IFRSs that are mandatorily effective for an accounting period that begins on or after January 1, 2014.

<u>Amendments to IFRS 10, IFRS 12 and IAS 27 Investment Entities</u>
Labrador Transco has applied the amendments to IFRS 10, IFRS 12 and IAS 27 Investment Entities for the first time in the current year. The amendments to IFRS 10 define an investment entity and require a reporting entity that meets the definition of an investment entity not to consolidate its subsidiaries but instead to measure its subsidiaries at fair value through profit or loss in its consolidated and separate financial statements.

To qualify as an investment entity, a reporting entity is required to:

- obtain funds from one or more investors for the purpose of providing them with investment management services;
- commit to its investor(s) that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both; and
- measure and evaluate performance of substantially all of its investments on a fair value basis.

Consequential amendments have been made to IFRS 12 and IAS 27 to introduce new disclosure requirements for investment entities.

Labrador Transco is not an investment entity (assessed based on the criteria set out in IFRS 10 as at January 1, 2014), the application of the amendments had no impact on the disclosures or the amounts recognized in Labrador Transco's financial statements.

Amendments to IAS 32 Offsetting Financial Assets and Financial Liabilities
Labrador Transco has applied the amendments to IAS 32 Offsetting Financial Assets and Financial Liabilities for the first time in the current year. The amendments to IAS 32 clarify the requirements relating to the offset of financial assets and financial liabilities. Specifically, the amendments clarify the meaning of 'currently has a legally enforceable right of set-off' and 'simultaneous realisation and settlement'.

As Labrador Transco does not have any financial assets and financial liabilities that qualify for offset, the application of the amendments had no impact on the disclosures or on the amounts recognized in Labrador Transco's financial statements.

Amendments to IAS 36 Recoverable Amount Disclosures for Non-Financial Assets
Labrador Transco has applied the amendments to IAS 36 Recoverable Amount Disclosures for Non-Financial Assets for the first time in the current year. The amendments to IAS 36 remove the requirement to disclose the recoverable amount of a CGU to which goodwill or other intangible assets with indefinite useful lives had been allocated when there has been no impairment or reversal of impairment of the related CGU. Furthermore, the amendments introduce additional disclosure requirements applicable to when the recoverable amount of an asset or a CGU is measured at fair value less costs of disposal. These new disclosures include the fair value hierarchy, key assumptions and valuation techniques used which are in line with the disclosure required by IFRS 13 Fair Value Measurements.

The application of these amendments had no material impact on the disclosures in Labrador Transco's financial statements.

Amendments to IAS 39 Novation of Derivatives and Continuation of Hedge Accounting
Labrador Transco has applied the amendments to IAS 39 Novation of Derivatives and Continuation of Hedge Accounting for the first time in the current year. The amendments to IAS 39 provide relief from the requirement to discontinue hedge accounting when a derivative designated as a hedging instrument is novated under certain circumstances. The amendments also clarify that any change to the fair value of the derivative designated as a hedging instrument arising from the novation should be included in the assessment and measurement of hedge effectiveness. As Labrador Transco does not have any derivatives that are subject to novation, the application of these amendments had no impact on the disclosures or on the amounts recognized in Labrador Transco's financial statements.

3. SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUMPTIONS

The preparation of the financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, revenues and expenses including, but not limited to, allocations of costs among entities. Actual results may materially differ from these estimates. The estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognized in the period in which the estimate is reviewed if the revision affects only that period or future periods.

3.1 Use of Judgment

Management applies its judgment when determining whether to consolidate structured entities in accordance with the criteria outlined in IFRS 10. Management has determined that Labrador Transco should not consolidate the Funding Trust.

4. FUTURE CHANGES IN ACCOUNTING POLICIES

Labrador Transco has not applied the following new and revised IFRSs that have been issued but are not yet effective:

IFRS 9	Financial Instruments[1]
IFRS 15	Revenue from Contracts with Customers[2]
Amendments to IAS 16 and IAS 38	Clarification of Acceptable Methods of Depreciation and Amortization[3]

[1]Effective for annual periods beginning on or after January 1, 2018, with earlier application permitted.
[2]Effective for annual periods beginning on or after January 1, 2017, with earlier application permitted.
[3]Effective for annual periods beginning on or after January 1, 2016, with earlier application permitted.

4.1 IFRS 9 – Financial Instruments

IFRS 9 issued in November 2009 introduced new requirements for the classification and measurement of financial assets. IFRS 9 was subsequently amended in October 2010 to include requirements for the classification and measurement of financial liabilities and for de-recognition, and in November 2013 to include the new requirements for general hedge accounting. Another revised version of IFRS 9 was issued in July 2014 mainly to include:

a) impairment requirements for financial assets, and
b) limited amendments to the classification and measurement requirements by introducing a 'fair value through other comprehensive income' (FVTOCI) measurement category for certain simple debt instruments

Key Requirements of IFRS 9:

- All recognized financial assets that are within the scope of IAS 39 Financial Instruments: Recognition and Measurement are required to be subsequently measured at amortized cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortized cost at the end of subsequent accounting periods. Debt instruments that are held within a business model whose objective is achieved both by collecting contractual cash flows and selling financial assets, and that have contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding, are measured at FVTOCI. All other debt investments and equity investments are measured at their fair value at the end of subsequent accounting periods. In addition, under IFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading) in other comprehensive income, with only dividend income generally recognized in profit or loss.

- With regard to the measurement of financial liabilities designated as at fair value through profit or loss, IFRS 9 requires that the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributes to a financial liability's credit risk are not subsequently reclassified to profit or loss. Under IAS 39, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss is presented in profit or loss.

- In relation to the impairment of financial assets, IFRS 9 requires an expected credit loss model, as opposed to an incurred credit loss model under IAS 39. The expected credit loss model requires an entity to account for expected credit losses and changes in those expected credit losses at each reporting date to reflect changes in credit risk since initial recognition. In other words, it is no longer necessary for a credit event to have occurred before credit losses are recognized.

- The new general hedge accounting requirements retain the three types of hedge accounting mechanisms currently available in IAS 39. Under IFRS 9, greater flexibility has been introduced to the types of transactions eligible for hedge accounting, specifically broadening the types of instruments that qualify for hedging instruments and the types of risk components of non-financial items that are eligible for hedge accounting. In addition, the effectiveness test has been overhauled and replaced with the principle of an 'economic relationship'. Retrospective assessment of hedge effectiveness is also no longer required. Enhanced disclosure requirements about an entity's risk management activities have also been introduced.

Management anticipates that the application of IFRS 9 in the future may have a material impact on amounts reported in respect of the Company's financial assets and financial liabilities. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 9 until Management undertakes a detailed review.

4.2 IFRS 15 Revenue from Contracts with Customers

In May 2014, IFRS 15 was issued and establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 18 Revenue, IAS 11 Construction Contracts and the related interpretations when it becomes effective.

The core principle of IFRS 15 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, the Standard introduces a five-step approach to revenue recognition:

Step 1: Identify the contract(s) with a customer.
Step 2: Identify the performance obligations in the contract.
Step 3: Determine the transaction price.
Step 4: Allocate the transaction price to the performance obligations in the contract.
Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

Under IFRS 15, an entity recognizes revenue when (or as) a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added in IFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by IFRS 15.

Management anticipates that the application of IFRS 15 in the future may have a material impact on the amounts reported and disclosures made in the Company's financial statements. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 15 until Management performs a detailed review.

4.3 Amendments to IAS 16 and IAS 38 Clarification of Acceptable Methods of Depreciation and Amortization

The amendments to IAS 16 prohibit entities from using revenue-based depreciation methods for items of property, plant and equipment. The amendments to IAS 38 introduce a rebuttable presumption that revenue is not an appropriate basis for amortization of an intangible asset. This presumption can only be rebutted in the following two limited circumstances:

a) when the intangible asset is expressed as a measure of revenue, or
b) when it can be demonstrated that revenue and consumption of the economic benefits of the intangible asset are highly correlated.

The amendments apply prospectively for annual periods beginning on or after January 1, 2016. Currently, the Company uses the straight-line method for depreciation for its property, plant and equipment. Management believes that the straight-line method is the most appropriate method to reflect the consumption of economic benefit inherent in the respective assets and accordingly does not anticipate that the application of these amendments to IAS 16 and IAS 38 will have a material impact on the Company's financial statements.

5. RESTRICTED CASH

Restricted cash is held in accounts administered by a Collateral Agent for the sole purpose of funding construction costs related to the LTA. The Company draws funds from this account on a monthly basis in accordance with procedures set out in the MF/LTA Project Finance Agreement (PFA).

6. TRADE AND OTHER RECEIVABLES

The composition of trade and other receivables is as follows:

(thousands of Canadian dollars)	**2014**	2013
Receivables due from related parties	**5,791**	97
Other receivables	**6,926**	5
	12,717	102

Other receivables are comprised primarily of government input tax credits and a small amount of accrued interest.

7. PROPERTY, PLANT AND EQUIPMENT

Capitalized costs related to the construction of the LTA are shown in the table below:

(thousands of Canadian Dollars)	Balance, January 1, 2014	Additions	Accumulated Depreciation	**Balance, December 31, 2014**
Project support assets	-	5,438	793	**4,645**
Construction in progress	126,702	189,934	-	**316,636**
	126,702	195,372	793	**321,281**

All amounts recorded in construction in progress relate to the development of the LTA. On November 30, 2013, Nalcor contributed construction in progress of $108.9 million to Labrador Transco. There were no additional contributions in 2014.

Capitalized Borrowing Costs
The construction of the LTA was sanctioned in December 2012. The construction is being financed through the issuance of long-term debt and contributed capital. During 2014, $11.6 million (2013 - $0.6 million) of borrowing costs were capitalized. The effective interest rate of the debt is 3.80%.

8. INVESTMENTS

In December 2013, the Company, jointly with Muskrat Falls, purchased three structured deposit notes using the proceeds from the issue of long-term debt. Labrador Transco recognizes its rateable share of 18% of these investments. Labrador Transco's rateable share was determined based on the percentage of the proceeds of long-term debt allocated for the construction of the LTA.

Details of the investments are as follows:

(thousands of Canadian dollars)	**2014**	2013
$75.0 million Floating Rate Deposit Note, with interest paid at the one-month Canadian Dealer Offer Rate (CDOR) plus 0.38%.	**13,500**	13,500
$478.2 million Amortizing Floating Rate Deposit Note, with interest paid at the One-Month CDOR plus 0.38%.	**42,249**	76,643
$1,912.7 million Amortizing Fixed Rate Deposit Note, with interest paid at a rate of 1.5937% per annum.	**168,997**	306,574
	224,746	396,717

9. TRADE AND OTHER PAYABLES

The composition of trade and other payables is as follows:

(thousands of Canadian dollars)	**2014**	2013
Trade payables	**56,871**	16,497
Payables due to related parties	**4,552**	1,603
Accrued interest payable	**1,480**	860
Other payables	**7**	-
	62,910	18,960

10. LONG-TERM DEBT

Details of the long-term debt are as follows:

(thousands of Canadian dollars)	**Face Value**	**Coupon Rate %**	**Year of Issue**	**Year of Maturity**	**2014**	2013
Tranche A	117,000	3.63	2013	2029	**117,039**	117,042
Tranche B	121,500	3.83	2013	2037	**121,519**	121,519
Tranche C	229,500	3.86	2013	2048	**229,544**	229,546
Total debentures	468,000				**468,102**	468,107

On November 29, 2013, Labrador Transco entered into the PFA with the Funding Trust and Muskrat Falls. Under the terms and conditions of the PFA, the Funding Trust agreed to provide a non-revolving credit facility in the amount of $2.6 billion available in three tranches (Tranches A, B and C). The purpose of the Funding Trust is to issue long-term debentures to the public, which debt is guaranteed by the Government of Canada and to on-lend the proceeds to Muskrat Falls and Labrador Transco. Muskrat Falls and Labrador Transco are both jointly and severally liable for the full amount of the credit facility.

On December 13, 2013, all three tranches of the construction facility were drawn down by way of a single advance of $2.6 billion. Under the terms of the PFA, the $2.6 billion advance is held in an account administered by a Collateral Agent. The Company draws funds from this account on a monthly basis in accordance with procedures set out in the PFA.

The role of the Collateral Agent is to act on behalf of the lending parties, including the Funding Trust and the Government of Canada. The Collateral Agent oversees the lending and security arrangements, the various project accounts and the compliance with covenants.

As security for these debt obligations, Labrador Transco has granted to the Collateral Agent first ranking liens on all present and future assets. On the date of the release of the final funding request to the Collateral Agent, sinking funds are required to be set up for each of the three tranches to be held in a sinking fund account under the control of the Collateral Agent.

Although Labrador Transco is jointly and severally liable for the $2.6 billion, only Labrador Transco's project ratable share of 18% is recognized as long-term debt.

11. SHAREHOLDER'S EQUITY

11.1 Share Capital

The share capital of Labrador Transco as at December 31 is summarized below:

(thousands of Canadian dollars)	**2014**	2013
Common shares without nominal or par value		
Authorized - unlimited		
Issued and outstanding - 100	**1**	1

11.2 Contributed Capital

(thousands of Canadian dollars)	**2014**	2013
Total contributed capital	**135,537**	107,631

During 2014, Nalcor contributed cash in the amount of $27.9 million as the first of four instalment payments to meet pre-funded equity requirements associated with the PFA (2013 – nil cash, $108.9 million in property, plant and equipment and $1.3 million in associated liabilities).

12. NET FINANCE INCOME AND EXPENSE

For the year ended December 31 (with comparatives for the one-month period ended December 31, 2013)	**2014**	2013
Finance income		
Interest on investments	**5,043**	210
Other interest income	**1,116**	97
	6,159	307
Finance expense		
Interest on long-term debt	**(17,769)**	(860)
Interest capitalized during construction	**11,610**	553
	(6,159)	(307)
Net finance income and expense	**-**	-

13. CAPITAL MANAGEMENT

Long-term capital includes share capital and contributed capital net of deficit. The Company's objectives for managing capital are to maintain its ability to continue as a going concern and to ensure timely payment of its contractual obligations as they relate to the construction of the LTA. Labrador Transco's future requirements for capital are expected to increase commensurate with progress on the construction. During this time, it is expected that proceeds from the Muskrat/LTA Construction Facility and contributed capital will be sufficient to fund the development of the LTA. Additional requirements will be funded entirely through contributed capital. Nalcor Energy, as well as the Province of Newfoundland and Labrador have provided guarantees of equity support in relation to the construction of the LTA. These guarantees, together with the proceeds from long-term debt will ensure sufficient funds are available to finance construction.

14. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

14.1 Fair Value

The estimated fair values of financial instruments as at December 31, 2014 and December 31, 2013 are based on relevant market prices and information available at the time. Fair value estimates are based on valuation techniques which are significantly affected by the assumptions used including the amount and timing of future cash flows and discount rates reflecting various degrees of risk. As such, the fair value estimates below are not necessarily indicative of the amounts that Labrador Transco might receive or incur in actual market transactions.

As a significant number of Labrador Transco's assets and liabilities do not meet the definition of a financial instrument, the fair value estimates below do not reflect the fair value of Labrador Transco as a whole.

<u>Establishing Fair Value</u>
Financial instruments recorded at fair value are classified using a fair value hierarchy that reflects the nature of the inputs used in making the measurements. The fair value hierarchy has the following levels:

Level 1 - valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 - valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices).

Level 3 - valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value. For assets and liabilities that are recognized at fair value on a recurring basis, the Company determines whether transfers have occurred between levels in the hierarchy by reassessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period. There were no transfers between Level 1, 2 and 3 fair value measurement during the years ended December 31, 2013 and December 31, 2014.

As of December 31, 2014 and December 31, 2013, the Company did not have any level 3 instruments.

(thousands of Canadian dollars)	Level	**Carrying Value**	**Fair Value**	Carrying Value	Fair Value
		2014		2013	
Financial assets					
Restricted cash	1	**106,032**	**106,032**	69,978	69,978
Trade and other receivables	1	**12,717**	**12,717**	102	102
Investments	2	**224,746**	**224,780**	396,717	396,650
Financial liabilities					
Trade and other payables	1	**62,910**	**62,910**	18,960	18,960
Long-term debt	2	**468,102**	**550,911**	468,107	475,870

The fair value of restricted cash, trade and other receivables and trade and other payables approximates their carrying values due to their short-term maturity.

14.2 Financial Risk Management

The Company is exposed to credit, liquidity and market risks through its operating, investing and financing activities.

(a) Credit Risk

The Company's expected future cash flows are exposed to credit risk through financing activities, based on the risk of non-performance by counterparties to financial instruments.

Credit risk on restricted cash and investments is minimal, as the Company's deposits and investments are held by a Canadian Schedule 1 Chartered Bank with a rating of AA- (Standard and Poor's).

The degree of exposure to credit risk on trade and other receivables and advances is determined by the financial capacity and stability of the counterparties whereby the maximum risk is represented by their carrying value on the Statement of Financial Position at the reporting date.

(b) Liquidity Risk

The Company is exposed to liquidity risk with respect to its contractual obligations and financial liabilities. Liquidity risk management activities are directed at ensuring cash is available to meet those obligations as they become due. Short-term liquidity is provided through restricted cash on hand. The Company can access the funds drawn down from the Muskrat/LTA Construction Facility for the payment of construction costs as well as interest payments.

The following are the contractual maturities of the Company's financial liabilities, including principal and interest, as at December 31, 2014:

(thousands of Canadian dollars)	< 1 Year	1-3 Years	3-5 Years	> 5 Years	Total
Trade and other payables	62,910	-	-	-	62,910
Long-term debt (including interest)	17,759	35,519	35,519	845,213	934,010
	80,669	35,519	35,519	845,213	996,920

(c) Market Risk

The Company is exposed to possible market price movements that could impact expected future cash flow and the carrying value of certain financial assets and liabilities.

Interest Rates

Changes in prevailing interest rates will impact the fair value of financial assets and liabilities. Expected future cash flows from these assets and liabilities are also impacted in certain circumstances.

Foreign Currency and Commodity Exposure

The Company does not hold any financial instrument whose value would vary due to changes in a commodity price or fluctuations in foreign currency exchange rates. Cash flow exposure to commodity price and foreign exchange risk arises primarily through investing activities, most notably US dollar denominated capital expenditures, and regular procurement activities. Exposure arising from capital expenditures is evaluated on a case by case basis. Where possible, contracts are denominated in Canadian dollars.

15. RELATED PARTY TRANSACTIONS

Labrador Transco enters into various transactions with its parent and other affiliates. These transactions occur in the normal course of operations and are measured at the exchange amount, which is the amount of consideration agreed to by the related parties. Related parties with which Labrador Transco transacts are as follows:

Related Party	Relationship
Nalcor Energy (Nalcor)	100% shareholder of Labrador Transco
Muskrat Falls	100% owned subsidiary of Nalcor
Funding Trust	Party to the PFA
Lower Churchill Management Corporation (LCMC)	100% owned subsidiary of Nalcor
Labrador-Island Link Limited Partnership	Limited partnership between Nalcor and Emera NL
Newfoundland and Labrador Hydro (Hydro)	100% owned subsidiary of Nalcor

In December 2014, Nalcor contributed $27.9 million to Labrador Transco as the first of four instalment payments to meet pre-funded equity requirements associated with the PFA. The funds are being held in an escrow account administered by the Collateral Agent.

16. COMMITMENTS AND CONTINGENCIES

(a) Labrador Transco has entered into the GIA with Muskrat Falls and Hydro, whereby Labrador Transco has committed to design, construct, operate and maintain the LTA, and provides such other services as agreed to ensure safe and reliable transmission of electricity.

(b) As part of the PFA, Labrador Transco has pledged its present and future assets as security to the Collateral Agent.

(c) Labrador Transco is subject to legal proceedings in the normal course of business. Although the outcome of such actions cannot be predicted with certainty, Management currently believes Labrador Transco’s exposure to such claims and litigation, to the extent not covered by insurance policies or otherwise provided for is not expected to materially affect its financial position.

(d) As at December 31, 2014, Labrador Transco had outstanding commitments for construction costs related to the LTA of $509.7.0 million.

17. SUPPLEMENTARY CASH FLOW INFORMATION

(thousands of Canadian dollars)	**2014**	2013
Trade and other receivables	**(12,615)**	(102)
Trade and other payables	**43,950**	17,684
Changes in non-cash working capital balances	**31,335**	17,582
Interest received	**6,132**	209
Interest paid	**17,044**	-

18. COMPARATIVE FIGURES

Certain comparative figures including prepayments, long-term prepayments and property, plant and equipment have been reclassified to conform to the presentation adopted during the current reporting period.