

MUSKRAT FALLS CORPORATION
CONDENSED INTERIM FINANCIAL STATEMENTS
March 31, 2017
(Unaudited)

MUSKRAT FALLS CORPORATION
STATEMENT OF FINANCIAL POSITION
(Unaudited)

<i>As at (thousands of Canadian dollars)</i>	Notes	March 31 2017	December 31 2016
ASSETS			
Current assets			
Restricted cash		348,618	287,797
Current portion of long-term investments	5	-	48,678
Current portion of advances	6	23,836	23,836
Trade and other receivables		25,316	47,607
Prepayments		3,254	3,254
Total current assets		401,024	411,172
Non-current assets			
Property, plant and equipment	3	3,320,860	3,158,742
Intangible assets	4	192	157
Advances	6	78,588	26,883
Long-term prepayments		1,002	1,815
Total assets		3,801,666	3,598,769
LIABILITIES AND EQUITY			
Current liabilities			
Trade and other payables		212,862	213,928
Non-current liabilities			
Long-term debt	7	2,054,401	2,054,407
Total liabilities		2,267,263	2,268,335
Shareholder's equity			
Share capital		1	1
Shareholder contributions	9	1,549,075	1,345,187
Reserves	8	(9,597)	(9,807)
Deficit		(5,076)	(4,947)
Total equity		1,534,403	1,330,434
Total liabilities and equity		3,801,666	3,598,769

Commitments and contingencies (Note 14)

See accompanying notes

MUSKRAT FALLS CORPORATION
STATEMENT OF LOSS AND COMPREHENSIVE INCOME
(Unaudited)

<i>For the period ended March 31 (thousands of Canadian dollars)</i>	Notes	Three months ended	
		2017	2016
Operating costs		94	87
Other expense	11	35	513
Loss for the period		(129)	(600)
Other comprehensive income for the period			
Reclassification adjustments related to:			
Fair value hedges recognized in profit or loss		210	210
<i>Total items that may or have been reclassified to profit or loss</i>		210	210
Total comprehensive income (loss) for the period		81	(390)

See accompanying notes

MUSKRAT FALLS CORPORATION
STATEMENT OF CHANGES IN EQUITY
(Unaudited)

<i>(thousands of Canadian dollars)</i>	Notes	Share Capital	Shareholder Contributions	Reserves	Deficit	Total
Balance at January 1, 2017		1	1,345,187	(9,807)	(4,947)	1,330,434
Loss for the period		-	-	-	(129)	(129)
Net change in fair value of cash flow hedges	8	-	-	210	-	210
Total comprehensive income (loss) for the period		-	-	210	(129)	81
Shareholder contributions	9	-	203,888	-	-	203,888
Balance at March 31, 2017		1	1,549,075	(9,597)	(5,076)	1,534,403
Balance at January 1, 2016		1	980,651	(10,646)	(3,769)	966,237
Loss for the period		-	-	-	(600)	(600)
Net change in fair value of cash flow hedges	8	-	-	210	-	210
Total comprehensive income (loss) for the period		-	-	210	(600)	(390)
Shareholder contributions	9	-	38,610	-	-	38,610
Balance at March 31, 2016		1	1,019,261	(10,436)	(4,369)	1,004,457

See accompanying notes

MUSKRAT FALLS CORPORATION
STATEMENT OF CASH FLOWS
(Unaudited)

<i>For the period ended March 31 (thousands of Canadian dollars)</i>	Notes	Three months ended	
		2017	2016
Operating activities			
Loss for the period		(129)	(600)
Adjusted for items not involving a cash flow:			
Amortization of long-term prepayments		813	813
Accretion of long-term debt		(6)	(5)
Reserves amortized to profit or loss	8	210	210
Changes in non-cash working capital balances	15	9	(12)
Net cash provided from operating activities		897	406
Investing activities			
Additions to property, plant and equipment	3	(162,048)	(149,195)
Additions to intangible assets	4	(105)	(58)
Increase in advances	6	(51,705)	-
Decrease in investments	5	48,678	74,726
Changes in non-cash working capital balances	15	21,216	(18,611)
Net cash used in investing activities		(143,964)	(93,138)
Financing activities			
(Increase) decrease in restricted cash		(60,821)	54,122
Increase in shareholder contributions	9	203,888	38,610
Net cash provided from financing activities		143,067	92,732
Net increase (decrease) in cash		-	-
Cash, beginning of period		-	-
Cash, end of period		-	-
Interest received		647	2,281
Interest paid		2	3

See accompanying notes

MUSKRAT FALLS CORPORATION
NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (Unaudited)

1. DESCRIPTION OF BUSINESS

Muskrat Falls Corporation (Muskrat Falls or the Company) was incorporated on November 13, 2013 under the laws of Newfoundland and Labrador. Muskrat Falls is a 100% owned subsidiary of Nalcor Energy (Nalcor). Muskrat Falls' head office is located at 500 Columbus Drive, St. John's, Newfoundland and Labrador, A1B 0M4, Canada.

Muskrat Falls was formed to design, develop, construct, finance and operate the Muskrat Falls hydroelectric facility rated at 824 megawatts.

Muskrat Falls has entered into a power purchase agreement (PPA) with Newfoundland and Labrador Hydro (Hydro) for the sale of energy and capacity from the Muskrat Falls hydroelectric plant until January 1, 2068. Muskrat Falls has also entered into the Generator Interconnection Agreement (GIA) with Hydro and Labrador Transmission Corporation (Labrador Transco) which governs the development and operation of the Labrador Transmission Assets connecting the Muskrat Falls plant to the existing hydroelectric facility in Churchill Falls. Under the terms of the GIA, Muskrat Falls is required to pay for all costs associated with the Labrador Transmission Assets. Under the terms of the PPA, Muskrat Falls will recover all costs associated with the Muskrat Falls hydroelectric facility as well as the costs incurred by Muskrat Falls under the GIA. Hydro's obligation to pay for the costs under the PPA is absolute, non-conditional and irrevocable.

2. SIGNIFICANT ACCOUNTING POLICIES

Statement of Compliance and Basis of Measurement

These condensed interim financial statements have been prepared in accordance with International Accounting Standards (IAS) 34 Interim Financial Reporting and have been prepared using accounting policies consistent with those used in the preparation of the annual audited financial statements for the year ended December 31, 2016.

These condensed interim financial statements do not include all of the disclosures normally found in Muskrat Falls' annual audited financial statements and should be read in conjunction with the annual audited financial statements.

These condensed interim financial statements have been prepared on a historical cost basis and are presented in Canadian dollars with all values rounded to the nearest thousand, except when otherwise noted. The Board of Directors of Muskrat Falls has delegated the authority to approve the condensed interim financial statements to the Audit Committee of the Board of Directors of Nalcor, which approved the statements on May 9, 2017.

MUSKRAT FALLS CORPORATION
NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (Unaudited)

3. PROPERTY, PLANT AND EQUIPMENT

<i>(thousands of Canadian dollars)</i>	Project Support Assets	Construction in Progress	Total
Cost			
Balance at January 1, 2016	185,478	2,074,877	2,260,355
Additions	-	1,014,645	1,014,645
Other adjustments	(1,647)	-	(1,647)
Balance at December 31, 2016	183,831	3,089,522	3,273,353
Additions	-	167,587	167,587
Other adjustments	(436)	-	(436)
Balance at March 31, 2017	183,395	3,257,109	3,440,504
Depreciation			
Balance at January 1, 2016	75,629	-	75,629
Depreciation	38,982	-	38,982
Balance at December 31, 2016	114,611	-	114,611
Depreciation	5,033	-	5,033
Balance at March 31, 2017	119,644	-	119,644
Carrying value			
Balance at January 1, 2016	109,849	2,074,877	2,184,726
Balance at December 31, 2016	69,220	3,089,522	3,158,742
Balance at March 31, 2017	63,751	3,257,109	3,320,860

Capitalized Borrowing Costs

The construction of the Muskrat Falls hydroelectric facility was sanctioned in December 2012. The construction is being financed through the issuance of long-term debt and contributed capital. For the period ended March 31, 2017, \$18.9 million (December 31, 2016 - \$76.6 million) of borrowing costs were capitalized. The effective interest rate of the debt is 3.80%.

MUSKRAT FALLS CORPORATION
NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (Unaudited)

4. INTANGIBLE ASSETS

<i>(thousands of Canadian dollars)</i>	Computer Software
Cost	
Balance at January 1, 2016	1,946
Additions	279
Balance at December 31, 2016	2,225
Additions	105
Balance at March 31, 2017	2,330
Amortization	
Balance at January 1, 2016	1,810
Amortization	258
Balance at December 31, 2016	2,068
Amortization	70
Balance at March 31, 2017	2,138
Carrying value	
Balance at January 1, 2016	136
Balance at December 31, 2016	157
Balance at March 31, 2017	192

5. INVESTMENTS

In December 2013, the Company, jointly with Labrador Transco, purchased three structured deposit notes using the proceeds from the issue of long-term debt. The investments were restricted in nature and subject to the provisions contained within the MF/LTA Project Finance Agreement (MF/LTA PFA). In July 2015, Muskrat Falls, Labrador Transco, the Muskrat Falls/Labrador Transmission Assets Funding Trust (MF/LTA Funding Trust) and the Collateral Agent executed an amendment to the MF/LTA PFA. Under the amended MF/LTA PFA Muskrat Falls recognizes its ratable share of these investments, which is based on its cumulative portion of actual debt drawn for the construction of the Muskrat Falls hydroelectric facility. As of March 31, 2017, Muskrat Falls' portion was 79% (December 31, 2016 – 79%). As of March 31, 2017, these investments were fully drawn down.

<i>As at (thousands of Canadian dollars)</i>	Year of Maturity	March 31 2017	December 31 2016
\$75.0 million Floating Rate Deposit Note, with interest paid at the one-month Canadian Dollar Offer Rate (CDOR) plus 0.38%.	2017	-	48,678
Long-term investments, end of period		-	48,678
Less: redemptions to be received within one year		-	48,678
		-	-

MUSKRAT FALLS CORPORATION
NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (Unaudited)

6. ADVANCES

Advances consist of deposits paid to a contractor on a long-term construction contract in relation to the Muskrat Falls hydroelectric facility. Advances are secured by a letter of credit from a Canadian Schedule 1 Chartered bank.

<i>As at (thousands of Canadian dollars)</i>	March 31 2017	December 31 2016
Total advances	102,424	50,719
Less: current portion	23,836	23,836
Total long-term advances	78,588	26,883

7. LONG-TERM DEBT

The following table represents the value of long-term debt measured at amortized cost:

<i>As at (thousands of Canadian dollars)</i>	Face Value	Coupon Rate %	Year of Issue	Year of Maturity	March 31 2017	December 31 2016
Tranche A	513,500	3.63	2013	2029	513,646	513,649
Tranche B	533,250	3.83	2013	2037	533,323	533,324
Tranche C	1,007,250	3.86	2013	2048	1,007,432	1,007,434
Total debentures	2,054,000				2,054,401	2,054,407

In July 2015, Muskrat Falls, Labrador Transco, the MF/LTA Funding Trust and the Collateral Agent executed an amendment to the MF/LTA PFA. Under the amendment, Muskrat Falls continues to be jointly and severally liable for the total credit facility, however Muskrat Falls' portion of the ratable share is based on its cumulative portion of actual debt drawn for the construction of the Muskrat Falls hydroelectric facility. As of March 31, 2017, Muskrat Falls' cumulative portion of actual debt drawn was 79% (December 31, 2016 – 79%).

8. ACCUMULATED OTHER COMPREHENSIVE INCOME

The components of, and changes in, accumulated other comprehensive income (loss) are as follows:

<i>(thousands of Canadian dollars)</i>	2017	2016
Cash flow hedges		
Balance at January 1	(9,807)	(10,646)
Reclassification adjustments for amounts recognized in profit or loss	210	210
Balance at March 31	(9,597)	(10,436)

9. SHAREHOLDER'S EQUITY

Shareholder Contributions

<i>As at (thousands of Canadian dollars)</i>	March 31 2017	December 31 2016
Total shareholder contributions	1,549,075	1,345,187

During 2017, Nalcor made contributions to Muskrat Falls in the amount of \$203.9 million (December 31, 2016 - \$364.5 million).

MUSKRAT FALLS CORPORATION
NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (Unaudited)

10. NET FINANCE EXPENSE

<i>For the period ended March 31 (thousands of Canadian dollars)</i>	Three months ended	
	2017	2016
Finance income		
Interest on investments	48	1,103
Other interest income	531	1,127
	579	2,230
Finance expense		
Interest on long-term debt	19,486	18,746
Bank fees	2	3
	19,488	18,749
Interest capitalized during construction	(18,909)	(16,519)
	579	2,230
Net finance expense	-	-

11. OTHER EXPENSE

<i>For the period ended March 31 (thousands of Canadian dollars)</i>	Three months ended	
	2017	2016
Realized foreign exchange loss	35	418
Unrealized foreign exchange loss	-	95
Other expense	35	513

12. FINANCIAL INSTRUMENTS

Fair Value

The estimated fair values of financial instruments as at March 31, 2017 and December 31, 2016 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 disclosed are not necessarily indicative of the amounts that Muskrat Falls might receive or incur in actual market transactions.

As a significant number of Muskrat Falls' assets and liabilities do not meet the definition of a financial instrument, the fair value estimates disclosed do not reflect the fair value of Muskrat Falls as a whole.

Establishing Fair Value

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).

MUSKRAT FALLS CORPORATION
NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (Unaudited)

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 measurements during the periods ended March 31, 2017 and December 31, 2016.

As at March 31, 2017 and December 31, 2016, the Company did not have any Level 3 instruments.

	Level	Carrying Value	Fair Value	Carrying Value	Fair Value
		March 31, 2017		December 31, 2016	
<i>(thousands of Canadian dollars)</i>					
Financial assets					
Investments	2	-	-	48,678	48,664
Financial liabilities					
Long-term debt	2	2,054,401	2,322,150	2,054,407	2,303,470

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

The fair values of Level 2 financial instruments are determined using quoted prices in active markets, which in some cases are adjusted for factors specific to the asset or liability. Level 2 fair values of other risk management assets and liabilities and long-term debt are determined using observable inputs other than unadjusted quoted prices, such as interest rate yield curves and currency rates.

13. RELATED PARTY TRANSACTIONS

Muskrat Falls 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 Muskrat Falls transacts are as follows:

Related Party	Relationship
Nalcor	100% shareholder of Muskrat Falls
Hydro	Wholly-owned subsidiary of Nalcor
Labrador Transco	Wholly-owned subsidiary of Nalcor
Lower Churchill Management Corporation (LCMC)	Wholly-owned subsidiary of Nalcor
Labrador-Island Link Limited Partnership (LIL LP)	Limited partnership between Labrador-Island Link Holding Corporation and Emera Newfoundland and Labrador Island Link Inc.
MF/LTA Funding Trust	Party to the MF/LTA PFA

Routine operating transactions with related parties are settled at prevailing market prices under normal trade terms.

- (a) As at March 31, 2017, Muskrat Falls has related party payables totaling \$3.8 million (December 31, 2016 - \$0.4 million) with Labrador Transco, LCMC and Nalcor and related party receivables totaling \$8.3 million (December 31, 2016 - \$1.9 million) with LIL LP. These payables and receivables consist of various intercompany operating and construction costs.
- (b) For the period ended March 31, 2017, Muskrat Falls has received contributions from Nalcor totaling \$203.9 million (March 31, 2016 – \$38.6 million).

MUSKRAT FALLS CORPORATION

NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (Unaudited)

14. COMMITMENTS AND CONTINGENCIES

- (a) Muskrat Falls has entered into the GIA with Labrador Transco and Hydro, whereby Muskrat Falls has committed to design, construct, operate and maintain the Muskrat Falls hydroelectric facility, and provide such other services as agreed to ensure safe and reliable transmission of electricity.
- (b) As part of the MF/LTA PFA, Muskrat Falls has pledged its present and future assets as security to the Collateral Agent.
- (c) Muskrat Falls 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 Muskrat Falls' 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) Outstanding commitments for capital projects, total approximately \$982.1 million as at March 31, 2017 (December 31, 2016 - \$1,100.3 million). Outstanding commitments related to pre-funded equity requirements associated with the Project Finance Agreements total approximately \$822.0 million as at March 31, 2017 (December 31, 2016 - \$1,765.1 million).

15. SUPPLEMENTARY CASH FLOW INFORMATION

<i>For the period ended March 31 (thousands of Canadian dollars)</i>	Three months ended	
	2017	2016
Trade and other receivables	22,291	2,084
Trade and other payables	(1,066)	(20,707)
Changes in non-cash working capital balances	21,225	(18,623)
Related to:		
Operating activities	9	(12)
Investing activities	21,216	(18,611)
	21,225	(18,623)