

**MUSKRAT FALLS CORPORATION**  
**CONDENSED INTERIM FINANCIAL STATEMENTS**  
**September 30, 2017**  
**(Unaudited)**

**MUSKRAT FALLS CORPORATION**  
**STATEMENT OF FINANCIAL POSITION**  
**(Unaudited)**

<i>As at (thousands of Canadian dollars)</i>	Notes	<b>September 30</b> <b>2017</b>	December 31 2016
<b>ASSETS</b>			
Current assets			
Restricted cash		<b>323,363</b>	287,797
Current portion of long-term investments	5	<b>582,179</b>	48,678
Current portion of advances	6	<b>79,454</b>	23,836
Trade and other receivables		<b>44,995</b>	47,607
Prepayments		<b>2,272</b>	3,254
<b>Total current assets</b>		<b>1,032,263</b>	411,172
Non-current assets			
Property, plant and equipment	3	<b>3,980,057</b>	3,158,742
Intangible assets	4	<b>239</b>	157
Long-term investments	5	<b>309,013</b>	-
Advances	6	<b>52,970</b>	26,883
Long-term prepayments		<b>355</b>	1,815
<b>Total assets</b>		<b>5,374,897</b>	3,598,769
<b>LIABILITIES AND EQUITY</b>			
Current liabilities			
Trade and other payables		<b>331,057</b>	213,928
Non-current liabilities			
Long-term debt	7	<b>3,561,834</b>	2,054,407
<b>Total liabilities</b>		<b>3,892,891</b>	2,268,335
Shareholder's equity			
Share capital		<b>1</b>	1
Shareholder contributions		<b>1,549,075</b>	1,345,187
Reserves	8	<b>(60,918)</b>	(9,807)
Deficit		<b>(6,152)</b>	(4,947)
<b>Total equity</b>		<b>1,482,006</b>	1,330,434
<b>Total liabilities and equity</b>		<b>5,374,897</b>	3,598,769

Commitments and contingencies (Note 13)

*See accompanying notes*

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

<i>For the period ended September 30 (thousands of Canadian dollars)</i>	Notes	Three months ended		Nine months ended	
		2017	2016	2017	2016
Operating costs		<b>222</b>	136	<b>493</b>	224
Other expense (income)	10	<b>(173)</b>	328	<b>712</b>	785
Loss for the period		<b>(49)</b>	(464)	<b>(1,205)</b>	(1,009)
Other comprehensive (loss) income for the period					
Cash flow hedges					
Net fair value losses on cash flow hedges		-	-	<b>(51,959)</b>	-
Reclassification adjustments for amounts recognized in profit or loss	8	<b>524</b>	210	<b>848</b>	629
<i>Total items that may or have been reclassified to profit or loss</i>		<b>524</b>	210	<b>(51,111)</b>	629
Total comprehensive (loss) income for the period		<b>475</b>	(254)	<b>(52,316)</b>	(380)

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
<b>Balance at January 1, 2017</b>		<b>1</b>	<b>1,345,187</b>	<b>(9,807)</b>	<b>(4,947)</b>	<b>1,330,434</b>
<b>Loss for the period</b>		-	-	-	<b>(1,205)</b>	<b>(1,205)</b>
<b>Net change in fair value of cash flow hedges</b>	<b>8</b>	-	-	<b>(51,111)</b>	-	<b>(51,111)</b>
<b>Total comprehensive loss for the period</b>		-	-	<b>(51,111)</b>	<b>(1,205)</b>	<b>(52,316)</b>
<b>Shareholder contributions</b>		-	<b>203,888</b>	-	-	<b>203,888</b>
<b>Balance at September 30, 2017</b>		<b>1</b>	<b>1,549,075</b>	<b>(60,918)</b>	<b>(6,152)</b>	<b>1,482,006</b>
Balance at January 1, 2016		1	980,651	(10,646)	(3,769)	966,237
Loss for the period		-	-	-	(1,009)	(1,009)
Net change in fair value of cash flow hedges	8	-	-	629	-	629
Total comprehensive income (loss) for the period		-	-	629	(1,009)	(380)
Shareholder contributions		-	263,507	-	-	263,507
Balance at September 30, 2016		1	1,244,158	(10,017)	(4,778)	1,229,364

See accompanying notes

**MUSKRAT FALLS CORPORATION**  
**STATEMENT OF CASH FLOWS**  
**(Unaudited)**

	Notes	Three months ended		Nine months ended	
		2017	2016	2017	2016
<i>For the period ended September 30 (thousands of Canadian dollars)</i>					
<b>Operating activities</b>					
Loss for the period		<b>(49)</b>	(464)	<b>(1,205)</b>	(1,009)
Adjustments for the following non-cash items					
Amortization of long-term prepayments		<b>78</b>	814	<b>1,460</b>	2,440
Accretion of long-term debt		<b>(22)</b>	(5)	<b>(40)</b>	(15)
Reserves amortized to profit or loss	8	<b>524</b>	210	<b>848</b>	629
Changes in non-cash working capital balances	14	<b>40</b>	24	<b>41</b>	13
<b>Net cash provided from operating activities</b>		<b>571</b>	579	<b>1,104</b>	2,058
<b>Investing activities</b>					
Additions to property, plant and equipment	3	<b>(357,392)</b>	(314,725)	<b>(821,083)</b>	(752,546)
Additions to intangible assets	4	<b>(82)</b>	(50)	<b>(314)</b>	(236)
Change in advances		-	-	<b>(81,705)</b>	55,293
Change in investments	5	<b>(891,192)</b>	87,365	<b>(842,514)</b>	256,441
Changes in non-cash working capital balances	14	<b>94,324</b>	(91,932)	<b>120,682</b>	(3,820)
<b>Net cash used in investing activities</b>		<b>(1,154,342)</b>	(319,342)	<b>(1,624,934)</b>	(444,868)
<b>Financing activities</b>					
Change in long-term debt	7	-	-	<b>1,507,467</b>	52,010
Change in restricted cash		<b>1,153,771</b>	217,260	<b>(35,566)</b>	127,293
Increase in shareholder contributions		-	101,503	<b>203,888</b>	263,507
Settlement of cash flow hedges	8	-	-	<b>(51,959)</b>	-
<b>Net cash provided from financing activities</b>		<b>1,153,771</b>	318,763	<b>1,623,830</b>	442,810
Net increase (decrease) in cash		-	-	-	-
Cash, beginning of period		-	-	-	-
Cash, end of period		-	-	-	-
Interest received		<b>5,196</b>	1,168	<b>6,516</b>	6,087
Interest paid		<b>2</b>	3	<b>38,248</b>	37,497

See accompanying notes

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

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**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 Standard (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 (CAD) 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 November 7, 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
<b>Additions</b>	<b>11,380</b>	<b>826,767</b>	<b>838,147</b>
<b>Other adjustments</b>	<b>(196)</b>	<b>-</b>	<b>(196)</b>
<b>Balance at September 30, 2017</b>	<b>195,015</b>	<b>3,916,289</b>	<b>4,111,304</b>
Depreciation			
Balance at January 1, 2016	75,629	-	75,629
Depreciation	38,982	-	38,982
Balance at December 31, 2016	114,611	-	114,611
<b>Depreciation</b>	<b>16,636</b>	<b>-</b>	<b>16,636</b>
<b>Balance at September 30, 2017</b>	<b>131,247</b>	<b>-</b>	<b>131,247</b>
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
<b>Balance at September 30, 2017</b>	<b>63,768</b>	<b>3,916,289</b>	<b>3,980,057</b>

Capitalized Borrowing Costs

The construction of the Muskrat Falls hydroelectric facility is being financed through the issuance of long-term debt and contributed capital. For the period ended September 30, 2017, \$69.5 million (December 31, 2016 - \$76.6 million) of borrowing costs were capitalized.

**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
<b>Additions</b>	<b>314</b>
<b>Balance at September 30, 2017</b>	<b>2,539</b>
Amortization	
Balance at January 1, 2016	1,810
Amortization	258
Balance at December 31, 2016	2,068
<b>Amortization</b>	<b>232</b>
<b>Balance at September 30, 2017</b>	<b>2,300</b>
Carrying value	
Balance at January 1, 2016	136
Balance at December 31, 2016	157
<b>Balance at September 30, 2017</b>	<b>239</b>

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

**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. These investments were fully drawn down in 2017. In July 2017, the Company, jointly with Labrador Transco, purchased three additional structured deposit notes using the proceeds from the issue of long-term debt. The investments are restricted in nature and subject to the provisions contained within the MF/LTA Project Finance Agreement (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 September 30, 2017, Muskrat Falls' portion was 80% (December 31, 2016 – 79%).

<i>As at (thousands of Canadian dollars)</i>	Year of Maturity	<b>September 30 2017</b>	December 31 2016
\$75.0 million Floating Rate Deposit Note, with interest paid at the one-month Canadian Dealer Offer Rate (CDOR) plus 0.38%.	2017	-	48,678
\$75.0 million Floating Rate Deposit Note, with interest paid at the one-month CDOR plus 0.20%.	2019	<b>60,000</b>	-
\$483.8 million Amortizing Floating Rate Deposit Note, with interest paid at the one-month CDOR plus 0.20%.	2019	<b>332,477</b>	-
\$725.7 million Amortizing Fixed Rate Deposit Note, with interest paid at a rate of 1.679% per annum.	2019	<b>498,715</b>	-
Long-term investments, end of period		<b>891,192</b>	48,678
Less: redemptions to be received within one year		<b>582,179</b>	48,678
		<b>309,013</b>	-

**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>	<b>September 30 2017</b>	December 31 2016
Total advances	<b>132,424</b>	50,719
Less: current portion	<b>79,454</b>	23,836
Total long-term advances	<b>52,970</b>	26,883



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

**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	September 30 2017	December 31 2016
Tranche A	520,000	3.63	2013	2029	<b>520,141</b>	513,649
Tranche B	540,000	3.83	2013	2037	<b>540,072</b>	533,324
Tranche C	1,020,000	3.86	2013	2048	<b>1,020,183</b>	1,007,434
Tranche 1-10	163,810	1.14-1.75	2017	2020-2025	<b>163,851</b>	-
Tranche 11-20	179,426	1.84-2.37	2017	2025-2030	<b>179,481</b>	-
Tranche 21-30	202,076	2.41-2.64	2017	2030-2035	<b>202,186</b>	-
Tranche 31-40	230,548	2.66-2.80	2017	2035-2040	<b>230,799</b>	-
Tranche 41-50	264,830	2.81-2.86	2017	2040-2045	<b>265,122</b>	-
Tranche 51-60	304,867	2.84-2.86	2017	2045-2050	<b>305,295</b>	-
Tranche 61-64	134,443	2.85	2017	2050-2052	<b>134,704</b>	-
<b>Total debentures</b>	<b>3,560,000</b>				<b>3,561,834</b>	<b>2,054,407</b>

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 Project Finance Agreement (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 September 30, 2017, Muskrat Falls' cumulative portion of actual debt drawn was 80% (December 31, 2016 – 79%). Cumulative adjustments were made in the current year to reflect Muskrat Falls' ratable share of the actual debt drawn.

On May 10, 2017, Muskrat Falls, Labrador Transco, the MF/LTA Funding Trust and the Collateral Agent executed a second amendment to the MF/LTA PFA. Under the terms and conditions of the second amended MF/LTA PFA, the MF/LTA Funding Trust agreed to provide an additional non-revolving credit facility in the amount of \$1.85 billion available in 64 series bonds with maturities of every six months beginning in December 2020. On May 25, 2017, the second construction facility was fully drawn down by way of a single advance to 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 MF/LTA PFA. The financing of the MF/LTA Funding Trust benefits from a direct, absolute, unconditional and irrevocable guarantee from Canada, and thereby carry its full faith and credit (AAA rating or equivalent). Under the terms of the additional guarantee from the Government of Canada, Muskrat Falls agree to pay an annual guarantee fee starting in May 2018 equal to its ratable share of 0.5% of the average balance outstanding on Tranches 1 through 64 for the prior twelve months.

As security for these debt obligations, Muskrat Falls has granted to the Collateral Agent first ranking liens on all present and future assets. Sinking funds are required to be set up for these debentures to be held in a sinking fund account under the control of the Collateral Agent.

Sinking fund installments due for the next five years for the 12 month period ended September 30 are as follows:

<i>(thousands of Canadian dollars)</i>	2018	2019	2020	2021	2022
Sinking fund instalments	-	-	-	57,778	57,778

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

**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>	<b>2017</b>	2016
Cash flow hedges		
Balance at January 1	<b>(9,807)</b>	(10,646)
Net fair value losses on cash flow hedges	<b>(51,959)</b>	-
Reclassification adjustments for amounts recognized in profit or loss	<b>848</b>	629
Balance at September 30	<b>(60,918)</b>	(10,017)

**9. NET FINANCE EXPENSE**

<i>For the period ended September 30 (thousands of Canadian dollars)</i>	<b>Three months ended</b>		<b>Nine months ended</b>	
	<b>2017</b>	2016	<b>2017</b>	2016
Finance income				
Interest on investments	<b>2,751</b>	457	<b>3,252</b>	3,241
Other interest income	<b>1,731</b>	633	<b>5,196</b>	2,748
	<b>4,482</b>	1,090	<b>8,448</b>	5,989
Finance expense				
Interest and fees on long-term debt	<b>31,628</b>	19,239	<b>77,966</b>	61,758
Bank fees	<b>2</b>	2	<b>6</b>	8
	<b>31,630</b>	19,241	<b>77,972</b>	61,766
Interest capitalized during construction	<b>(27,148)</b>	(18,151)	<b>(69,524)</b>	(55,777)
	<b>4,482</b>	1,090	<b>8,448</b>	5,989
Net finance expense	-	-	-	-

Due to the MF/LTA PFA amendment in July 2015, cumulative adjustments were made in the current year to net finance expense to reflect Muskrat Falls' ratable share of the actual debt drawn.

**10. OTHER EXPENSE (INCOME)**

<i>For the period ended September 30 (thousands of Canadian dollars)</i>	<b>Three months ended</b>		<b>Nine months ended</b>	
	<b>2017</b>	2016	<b>2017</b>	2016
Cash flow hedge ineffectiveness	<b>(0)</b>	-	<b>866</b>	-
Realized foreign exchange (gain) loss	<b>(188)</b>	167	<b>(172)</b>	607
Unrealized foreign exchange loss	<b>15</b>	161	<b>18</b>	178
Other expense (income)	<b>(173)</b>	328	<b>712</b>	785

**11. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT**

**11.1 Fair Value**

The estimated fair values of financial instruments as at September 30, 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.

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

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).

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 September 30, 2017 and December 31, 2016.

As at September 30, 2017 and December 31, 2016, the Company did not have any Level 3 instruments.

	Level	Category	Carrying Value	Fair Value	Carrying Value	Fair Value
			September 30, 2017		December 31, 2016	
<i>(thousands of Canadian dollars)</i>						
Financial assets						
Investments	2	HTM <sup>1</sup>	891,192	891,192	48,678	48,664
Financial liabilities						
Long-term debt	2	OFL <sup>2</sup>	3,561,834	3,708,424	2,054,407	2,303,470

<sup>1</sup>Held-to-maturity investments

<sup>2</sup>Other financial liabilities

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 long-term debt are determined using observable inputs other than unadjusted quoted prices, such as interest rate yield curves.

**11.2 Risk Management**

The Company is exposed to certain credit, liquidity and market risks through its operating, financing and investing activities. Financial risk is managed in accordance with a Board-approved policy, which outlines the objectives and strategies for the management of financial risk, including the use of derivative contracts. Permitted financial risk management strategies are aimed at minimizing the volatility of the Company's expected future cash flows.

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 Canadian Schedule 1 Chartered Banks with ratings of A and 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.

## MUSKRAT FALLS CORPORATION

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (Unaudited)

#### Liquidity Risk

The Company is exposed to liquidity risk with respect to its contractual obligations and financial liabilities, including derivative liabilities relating to hedging activities. 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 and shareholder contributions. The Company can access the funds drawn down from the Muskrat/LTA Construction Facility and shareholder contributions 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, sinking fund and interest as at September 30, 2017:

<i>(thousands of Canadian dollars)</i>	< 1 Year	1-3 Years	3-5 Years	> 5 Years	Total
Trade and other payables	331,057	-	-	-	331,057
Long-term debt (including interest and sinking fund)	116,645	233,291	412,122	5,500,935	6,262,993
	447,702	233,291	412,122	5,500,935	6,594,050

#### Market Risk

In the course of carrying out its operating, financing and investing activities, 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 instruments 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 and Euro 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 CAD.

### **11.3 Hedge Accounting**

In May 2017, Muskrat Falls entered into three bond forward contracts totaling \$1.4 billion to hedge the interest rate risk on the forecasted issue of the additional long-term debt. These contracts were designated as part of a cash flow hedging relationship and the resulting change in fair value was recorded in other comprehensive income (loss) with the ineffective portion recognized immediately in other (income) expense. The amortization of the other comprehensive loss related to the effective portion of the cash flow hedge is capitalized in line with treatment of the interest expense related to the long-term debt that it is hedging, until project commissioning. Subsequent to commissioning, amortization on the remainder of the effective portion will be recognized in profit or loss over the same period as the related debt instruments mature. The total amount amortized as at September 30, 2017 including the previous cash flow hedge initiated in December 2013 was \$0.8 million (December 31, 2016 - \$0.8 million).

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

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**12. RELATED PARTY TRANSACTIONS**

Musktrat 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 Musktrat Falls transacts are as follows:

Related Party	Relationship
Nalcor	100% shareholder of Musktrat 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.

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

- (a) As at September 30, 2017, Musktrat Falls has related party payables totaling \$14.9 million (December 31, 2016 - \$0.4 million) with LCMC and Nalcor and related party receivables totaling \$15.2 million (December 31, 2016 - \$1.9 million) with LIL LP and Labrador Transco. These payables and receivables consist of various intercompany operating and construction costs.
- (b) During 2017, Musktrat Falls has received contributions from Nalcor totaling \$203.9 million (September 30, 2016 – \$263.5 million).

**13. COMMITMENTS AND CONTINGENCIES**

- (a) Musktrat Falls has entered into the GIA with Labrador Transco and Hydro, whereby Musktrat Falls has committed to design, construct, operate and maintain the Musktrat 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, Musktrat Falls has pledged its present and future assets as security to the Collateral Agent.
- (c) In July 2012 Nalcor entered into the Energy and Capacity Agreement with Emera Inc. (Emera) providing for the sale and delivery of the Nova Scotia Block, 0.986 TWh of energy annually for a term of 35 years. In October 2015 Nalcor assigned this agreement to Musktrat Falls. As a result of this assignment, Nalcor and Musktrat Falls are jointly liable for the delivery of the Nova Scotia Block to Emera.
- (d) Musktrat 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 Musktrat 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.
- (e) Outstanding commitments for capital projects, total approximately \$767.5 million as at September 30, 2017 (December 31, 2016 - \$1,100.3 million). Outstanding commitments related to the Project Finance Agreements total approximately \$1,256.5 million as at September 30, 2017 (December 31, 2016 - \$1,765.1 million).

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

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**14. SUPPLEMENTARY CASH FLOW INFORMATION**

<i>For the period ended September 30 (thousands of Canadian dollars)</i>	<b>Three months ended</b>		<b>Nine months ended</b>	
	<b>2017</b>	2016	<b>2017</b>	2016
Trade and other receivables	<b>704</b>	(33,413)	<b>2,612</b>	(26,223)
Prepayments	<b>736</b>	-	<b>982</b>	-
Trade and other payables	<b>92,924</b>	(58,495)	<b>117,129</b>	22,416
Changes in non-cash working capital balances	<b>94,364</b>	(91,908)	<b>120,723</b>	(3,807)
Related to:				
Operating activities	<b>40</b>	24	<b>41</b>	13
Investing activities	<b>94,324</b>	(91,932)	<b>120,682</b>	(3,820)
	<b>94,364</b>	(91,908)	<b>120,723</b>	(3,807)