

**LOWER CHURCHILL PROJECT COMPANIES
COMBINED FINANCIAL STATEMENTS
December 31, 2019**

Independent Auditor's Report

To the Directors of Nalcor Energy

We have audited the accompanying combined financial statements of the Lower Churchill Project Companies (the "Company"), which comprise the combined statement of financial position as at December 31, 2019 and the combined statements of loss and comprehensive loss, changes in equity and cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies and other explanatory information. The combined financial statements have been prepared by management of the Lower Churchill Project Companies based on the financial reporting provisions of the Government of Newfoundland and Labrador Muskrat Falls Oversight Committee.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2019, and its financial performance and its cash flows for the year then ended in accordance with the financial reporting provisions of the Government of Newfoundland and Labrador Muskrat Falls Oversight Committee.

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards ("Canadian GAAS"). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Emphasis of Matter

We draw attention to Note 2 to the financial statements, which describes the basis of accounting. The combined financial statements are prepared to assist Nalcor Energy to comply with the financial reporting provisions of the Government of Newfoundland and Labrador Muskrat Falls Oversight Committee. As a result, the financial statements may not be suitable for another purpose. Our opinion is not modified in respect of this matter.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with the financial reporting provisions of the Government of Newfoundland and Labrador Muskrat Falls Oversight Committee, 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.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian GAAS will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Canadian GAAS, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Deloitte LLP

Chartered Professional Accountants
February 28, 2020

**LOWER CHURCHILL PROJECT COMPANIES
COMBINED STATEMENT OF FINANCIAL POSITION**

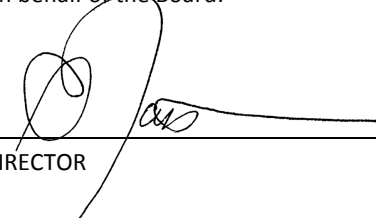
<i>As at December 31 (thousands of Canadian dollars)</i>	Notes	2019	2018
ASSETS			
Current assets			
Cash		1,620	5,567
Restricted cash		1,459,742	1,421,590
Investments	5	-	297,830
Trade and other receivables	6	18,415	220,742
Current portion of advances	7	24,899	25,028
Prepayments		8,245	10,597
Total current assets		1,512,921	1,981,354
Non-current assets			
Property, plant and equipment	8	10,976,487	10,036,356
Intangible assets	9	35,925	35,249
Advances	7	-	895
Long-term prepayments		-	7,159
Right-of-use assets	10	4,142	-
Total assets		12,529,475	12,061,013
LIABILITIES AND EQUITY			
Current liabilities			
Trade and other payables	11	212,695	295,162
Current portion of long-term debt	12	30,411	-
Current portion of lease liabilities	13	1,388	-
Total current liabilities		244,494	295,162
Non-current liabilities			
Long-term debt	12	7,873,388	7,903,983
Deferred revenue	14	52,300	36,500
Class B limited partnership units	15	578,368	533,058
Lease liabilities	13	2,827	-
Contributions		10	10
Total liabilities		8,751,387	8,768,713
Shareholder's equity			
Share capital	16	4	4
Shareholder contributions		3,864,696	3,369,035
Reserves		(66,452)	(70,174)
Deficit		(20,160)	(6,565)
Total equity		3,778,088	3,292,300
Total liabilities and equity		12,529,475	12,061,013

Commitments and contingencies (Note 23)

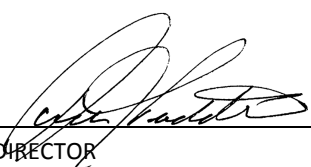
Subsequent event (Note 26)

See accompanying notes

On behalf of the Board:



DIRECTOR



DIRECTOR

LOWER CHURCHILL PROJECT COMPANIES
COMBINED STATEMENT OF (LOSS) PROFIT AND COMPREHENSIVE (LOSS) INCOME

<i>For the year ended December 31 (thousands of Canadian dollars)</i>	Notes	2019	2018
Other revenue	22	390	390
Operating costs	18	7,874	3,124
Other expense	19	59	188
Net finance expense (income)	17	6,042	(4,130)
Expenses		13,975	(818)
(Loss) profit for the year		(13,585)	1,208
Distribution of income	20	(10)	(10)
Other comprehensive income			
Total items that may or have been reclassified to profit or loss:			
Reclassification adjustment related to:			
Cash flow hedges recognized in profit or loss		3,722	3,721
Other comprehensive income for the year		3,722	3,721
Total comprehensive (loss) income for the year		(9,873)	4,919

See accompanying notes

**LOWER CHURCHILL PROJECT COMPANIES
COMBINED STATEMENT OF CHANGES IN EQUITY**

<i>(thousands of Canadian dollars)</i>	Notes	Share Capital	Shareholder Contributions	Reserves	Deficit	Total
Balance at January 1, 2019		4	3,369,035	(70,174)	(6,565)	3,292,300
Loss for the year		-	-	-	(13,585)	(13,585)
Distribution of income		-	-	-	(10)	(10)
Other comprehensive income		-	-	3,722	-	3,722
Total comprehensive profit (loss) for the year		-	-	3,722	(13,595)	(9,873)
Shareholder contributions	22	-	495,661	-	-	495,661
Balance at December 31, 2019		4	3,864,696	(66,452)	(20,160)	3,778,088
Balance at January 1, 2018		4	2,839,620	(73,895)	(7,763)	2,757,966
Profit for the year		-	-	-	1,208	1,208
Distribution of income		-	-	-	(10)	(10)
Other comprehensive income		-	-	3,721	-	3,721
Total comprehensive income for the year		-	-	3,721	1,198	4,919
Shareholder contributions	22	-	529,415	-	-	529,415
Balance at December 31, 2018		4	3,369,035	(70,174)	(6,565)	3,292,300

See accompanying notes

LOWER CHURCHILL PROJECT COMPANIES COMBINED STATEMENT OF CASH FLOWS

<i>For the year ended December 31 (thousands of Canadian dollars)</i>	Notes	2019	2018
Operating activities			
(Loss) profit for the year		(13,585)	1,208
Adjustments to reconcile (loss) profit to cash used in operating activities:			
Finance income	17	(30,105)	(33,449)
Finance expense	17	36,147	29,319
Amortization of prepayments		11,183	6,299
Gain on disposal of property, plant and equipment		(233)	-
Reserves amortized to profit or loss		3,722	3,721
		7,129	7,098
Increase in prepayments		(953)	(23,192)
Changes in non-cash working capital balances	25	(14,307)	1,420
Interest received		30,146	44,984
Interest paid		(279,410)	(291,633)
Net cash used in operating activities		(257,395)	(261,323)
Investing activities			
Additions to property, plant and equipment		(650,730)	(804,482)
Additions to intangible assets	9	(1,231)	(2,409)
Change in advances		1,024	51,660
Redemption of investments		297,830	1,037,684
Changes in non-cash working capital balances	25	134,686	(175,530)
Proceeds on disposal of property, plant and equipment		233	-
Net cash (used in) provided from investing activities		(218,188)	106,923
Financing activities			
Change in restricted cash		(38,152)	(385,069)
Change in deferred revenue	22	15,800	11,600
Increase in shareholder contributions	22	495,661	529,415
Distribution of income		(10)	(10)
Repayment of lease liabilities		(1,663)	-
Net cash provided from financing activities		471,636	155,936
Net (decrease) increase in cash		(3,947)	1,536
Cash, beginning of the year		5,567	4,031
Cash, end of the year		1,620	5,567

See accompanying notes

LOWER CHURCHILL PROJECT COMPANIES

NOTES TO COMBINED FINANCIAL STATEMENTS

1. NATURE AND DESCRIPTION OF THE PROJECT

These audited combined financial statements include the financial information of the consolidated Labrador-Island Link Holding Corporation (LIL Holdco), Muskrat Falls Corporation (Muskrat Falls), Labrador Transmission Corporation (Labrador Transco) and the Lower Churchill Management Corporation (LCMC). Collectively, the financial information from these combined companies is referred to as the Lower Churchill Project Companies (the Project).

Each of the entities was separately formed under the laws of the Province of Newfoundland and Labrador. LIL Holdco was formed on July 31, 2012, whereas Muskrat Falls, Labrador Transco and LCMC were formed on November 13, 2013.

The Project was established to carry on the business of designing, engineering, constructing, commissioning, owning, financing, operating and maintaining the assets and property constituting the Labrador-Island Link (LIL), the Labrador Transmission Assets (LTA) and the Muskrat Falls (MF) hydroelectric facility.

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 MF hydroelectric facility. Muskrat Falls and Labrador Transco have also entered into the Generator Interconnection Agreement (GIA) with Hydro which governs the development and operation of the LTA connecting the MF hydroelectric facility to the existing hydroelectric facility in Churchill Falls. 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 PPA with Hydro. Hydro's obligation to pay for the costs under the PPA is absolute, non-conditional and irrevocable.

Labrador-Island Link Partnership (the Partnership or LIL LP) has entered into the LIL Lease and the Transmission Funding Agreement (TFA) with Labrador-Island Link Operating Corporation (LIL Opco) and Hydro. These agreements effectively provide Hydro with transmission services over the LIL. LIL Opco will maintain and operate the LIL on behalf of the Partnership.

2. SIGNIFICANT ACCOUNTING POLICIES

2.1 Statement of Compliance and Basis of Measurement

These annual audited combined financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB), with the exception of the fact that these statements are combined as described in Note 1. The Project has adopted accounting policies which are based on IFRS applicable as at December 31, 2019, and includes individual IFRS, International Accounting Standards (IAS), and interpretations made by the IFRS Interpretations Committee and the Standing Interpretations Committee.

These annual audited combined 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 annual audited combined financial statements reflect the financial position and financial performance of the Project and do not include other assets, liabilities, revenues, and expenses of the partners of LIL LP. These annual audited combined financial statements were approved by Nalcor Energy's (Nalcor) Board of Directors on February 28, 2020.

2.2 Basis of Consolidation

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

- 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 variable returns.

LOWER CHURCHILL PROJECT COMPANIES

NOTES TO COMBINED FINANCIAL STATEMENTS

Based on the criteria outlined in IFRS 10, the Project has determined that LIL Holdco controls the LIL LP and LIL LP controls the LIL Construction Project Trust (Project Trust or the IT) for financial reporting purposes. The IT is a structured entity created for the purpose of obtaining financing and lending the proceeds to LIL LP. LIL LP used judgment in assessing many factors to determine control of the IT, including its exposure to variability in the IT's investments and its role in the formation of the IT. The Project has determined that Muskrat Falls and Labrador Transco are not the primary beneficiaries of the Muskrat Falls/Labrador Transmission Assets Funding Trust (MF/LTA Funding Trust) and that the LIL LP does not control the Labrador-Island Link Funding Trust (LIL Funding Trust) and has not included the results of the funding trusts in these audited combined financial statements.

2.3 Cash

Cash consists of amounts on deposit with a Schedule 1 Canadian Chartered Bank.

2.4 Restricted Cash

Restricted cash consists of cash held on deposit with Schedule 1 Canadian Chartered Banks and administered by the Collateral Agent for the sole purpose of funding construction costs related to the LIL, LTA and MF hydroelectric facility, including pre-funded equity amounts required under the LIL Project Finance Agreement (LIL PFA) and MF/LTA Project Finance Agreement (MF/LTA PFA). The Project draws funds from these accounts in accordance with procedures set out in the LIL PFA and the MF/LTA PFA. Restricted cash also includes accounts administered by the Administrator of the IT and funds held in trust by solicitors of the Project.

2.5 Property, Plant and Equipment

Items of property, plant and equipment are recognized at cost less accumulated depreciation and accumulated impairment losses. Cost includes materials, labour, contracted services, professional fees and, for qualifying assets, borrowing costs capitalized in accordance with the Project's accounting policy outlined in Note 2.7. Costs capitalized with the related asset include all costs directly attributable to bringing the asset into operation.

When significant parts of property, plant and equipment are required to be replaced at intervals, the Project recognizes such parts as individual assets with specific useful lives and depreciation rates, respectively. Likewise, when a major inspection is performed, its cost is recognized in the carrying amount of the plant and equipment as a replacement if the recognition criteria are satisfied. All other repairs and maintenance costs are recognized in profit or loss as incurred.

Depreciation of these assets commences when the assets are ready for their intended use. Residual values, useful lives and method of depreciation are reviewed at the end of year and adjusted prospectively, if appropriate. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets as follows:

Project support assets	4 - 7 years
Service facilities and other assets	7 - 45 years

As use of the project support assets is directly attributable to the construction of the LIL, LTA and MF hydroelectric facility, related depreciation costs are capitalized as incurred, until such time as the assets are substantially ready for their intended use or sale.

2.6 Intangible Assets

Intangible assets that are expected to generate future economic benefit and are measurable, including computer software costs and assets under development, are capitalized as intangible assets in accordance with IAS 38.

LOWER CHURCHILL PROJECT COMPANIES

NOTES TO COMBINED FINANCIAL STATEMENTS

Intangible assets with finite useful lives are carried at cost less accumulated amortization and accumulated impairment losses. Computer software is amortized on a straight-line basis over their finite useful lives of one year. Amortization of assets under development will commence once the LIL, LTA and MF hydroelectric facility are available for use and will be amortized over the term of the GIA/PPA and TFA. As use of the intangible assets is directly attributable to the construction of the LIL, LTA and MF hydroelectric facility, related amortization costs are capitalized as incurred. The estimated useful life and amortization method are reviewed at the end of each reporting year, with the effect of any changes in estimate being accounted for on a prospective basis. Intangible assets with indefinite useful lives are carried at cost less accumulated impairment losses.

2.7 Borrowing Costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that 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 the Combined Statement of (Loss) Profit and Comprehensive (Loss) Income in the period in which they are incurred.

2.8 Impairment of Non-Financial Assets

Property and equipment and other non-financial assets are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

Where it is not possible to estimate the recoverable amount of an individual asset, the Project estimates the recoverable amount of the cash generating unit (CGU) to which the asset belongs. 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. Value in use is generally computed by reference to the present value of future cash flows expected to be derived from non-financial assets.

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 the Combined Statement of (Loss) Profit and Comprehensive (Loss) Income.

2.9 Provisions

A provision is a liability of uncertain timing or amount. A provision is recognized if the Project 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 the current market assessments of the time value of money and the risks specific to the obligation. Provisions are re-measured at each Combined Statement of Financial Position date using the current discount rate.

2.10 Revenue Recognition

Revenue is recognized on an accrual basis as earned, when recovery is probable and the amount of revenue can be reliably measured.

LOWER CHURCHILL PROJECT COMPANIES

NOTES TO COMBINED FINANCIAL STATEMENTS

2.11 Leasing

Lessee Accounting

The Project assesses whether a contract is or contains a lease, at inception of a contract. The Project recognizes a right-of-use asset and a corresponding lease liability with respect to all lease agreements in which it is the lessee, except for short-term leases (defined as leases with a lease term of 12 months or less) and leases of low-value assets. For these leases, the Project would normally recognize the lease payments as an operating expense on a straight-line basis over the term of the lease unless another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. However, as the Project is still in the construction phase of its operations, lease payments are subsequently capitalized within property, plant and equipment when permitted by *IAS 16 – Property, Plant and Equipment*.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted by using the rate implicit in the lease. If this rate cannot be readily determined, the Project uses its incremental borrowing rate.

Lease payments included in the measurement of the lease liability comprise:

- fixed (and in-substance) lease payments less any lease incentives;
- variable lease payments that depend on an index or rate; and
- payments expected under residual value guarantees and payments relating to purchase options and renewal option periods that are reasonably certain to be exercised (or periods subject to termination options that are not reasonably certain to be exercised).

The lease liability is subsequently measured at amortized cost using the effective interest rate method. Lease liabilities are remeasured, with a corresponding adjustment to the related right-of-use assets, when there is a change in variable lease payments arising from a change in an index or rate, or when the Project changes its assessment of whether purchase, renewal or termination options will be exercised.

The Project did not make any such adjustments during the periods presented.

The right-of-use assets comprise the initial measurement of the corresponding lease liability, lease payments made at or before the commencement day and any initial direct costs. They are subsequently measured at cost less accumulated depreciation and accumulated impairment losses.

Whenever the Project incurs an obligation for costs to dismantle and remove a leased asset, restore the site on which it is located or restore the underlying asset to the condition required by the terms and conditions of the lease, a provision is recognized and measured under *IAS 37 - Provisions, Contingent Liabilities and Contingent Assets*. The costs are included in the related right-of-use asset.

Right-of-use assets are depreciated over the shorter period of the lease term and useful life of the underlying asset. If a lease transfers ownership of the underlying asset or the cost of the right-of-use asset reflects that the Project expects to exercise a purchase option, the related right-of-use asset is depreciated over the useful life of the underlying asset. Depreciation starts at the commencement date of the lease.

Variable rents that do not depend on an index or rate are not included in the measurement of the lease liability and the right-of-use asset. The related payments would normally be recognized as an expense in operating costs in the period in which the event or condition that triggers those payments occurs. However, as the Project is still in the construction phase of its operations, these payments are subsequently capitalized within property, plant and equipment when permitted by *IAS 16*.

As a practical expedient, *IFRS 16* permits a lessee not to separate non-lease components, and instead account for any lease and associated non-lease components as a single arrangement. The Project has elected to apply this practical expedient.

LOWER CHURCHILL PROJECT COMPANIES

NOTES TO COMBINED FINANCIAL STATEMENTS

2.12 Foreign Currencies

Transactions in currencies other than the Project's functional currency (foreign currencies) are recognized using the exchange rate in effect at the date of transaction, approximated by 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 are included in the Combined Statement of (Loss) Profit and Comprehensive (Loss) Income as other expense.

2.13 Income Taxes

Provision has not been made in LIL LP's annual audited consolidated financial statements for Canadian federal, provincial, or local taxes since any such liabilities are the responsibility of the individual partners. LCMC, Muskrat Falls, Labrador Transco and LIL Holdco are exempt from paying income taxes under section 149(1) (d.2) of the Income Tax Act.

2.14 Financial Instruments

Classification and Initial Measurement

Financial assets and financial liabilities are recognized in the Combined Statement of Financial Position when the Project becomes a party to the contractual provisions of the instrument and are initially measured at fair value.

Financial assets are classified at amortized cost, fair value through other comprehensive income (FVTOCI), fair value through profit or loss (FVTPL) or as derivatives designated as hedging instruments in an effective hedge. Financial liabilities are classified as financial liabilities designated at FVTPL, amortized cost or as derivatives designated as hedging instruments in an effective hedge. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at FVTPL) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at FVTPL are recognized immediately in profit or loss.

Financial Assets at Amortized Cost

Financial assets with contractual cash flows arising on specified dates, consisting solely of principal and interest, and that are held within a business model whose objective is to collect the contractual cash flows are subsequently measured at amortized cost using the effective interest rate method and are subject to impairment. Gains and losses are recognized in profit or loss when the asset is derecognized, modified or impaired.

The Project's financial assets at amortized cost include cash, restricted cash, investments, trade and other receivables and advances.

Financial Liabilities at Amortized Cost

The Project subsequently measures all financial liabilities at amortized cost using the effective interest rate method. Gains and losses are recognized in profit or loss when the liability is derecognized.

The Project's financial liabilities at amortized cost include trade and other payables and long-term debt.

Derecognition of Financial Instruments

The Project derecognizes a financial asset 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 party.

The Project derecognizes financial liabilities when, and only when, its obligations are discharged, cancelled or have expired. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in profit or loss.

Impairment of Financial Assets

The Project recognizes a loss allowance for expected credit losses (ECL) on investments in debt instruments that are measured at amortized cost or at FVTOCI. The amount of ECL is updated at each reporting date to reflect changes in

LOWER CHURCHILL PROJECT COMPANIES

NOTES TO COMBINED FINANCIAL STATEMENTS

credit risk since initial recognition of the respective financial instrument.

The Project always recognizes lifetime ECL for trade and other receivables. The ECL on these financial assets are estimated based on the Project's historical credit loss experience, adjusted for factors that are specific to the debtors, general economic conditions and an assessment of both the current as well as the forecast direction of conditions at the reporting date, including time value of money where appropriate. The Project also records 12-month ECL for those financial assets which have low credit risk and where the low credit risk exemption has been applied. The classes of financial assets that have been identified to have low credit risk consist of cash, restricted cash, investments and advances.

For all other financial instruments, the Project recognizes lifetime ECL when there has been a significant increase in credit risk since initial recognition. If, on the other hand, the credit risk on the financial instrument has not increased significantly since initial recognition, the Project measures the loss allowance for that financial instrument at an amount equal to 12-month ECL. The assessment of whether lifetime ECL should be recognized is based on significant increases in the likelihood or risk of a default occurring since initial recognition instead of on evidence of a financial asset being credit-impaired at the reporting date or an actual default occurring.

Lifetime ECL represents the ECL that will result from all possible default events over the expected life of a financial instrument. In contrast, 12-month ECL represents the portion of lifetime ECL that is expected to result from default events on a financial instrument that are possible within 12 months after the reporting date.

Hedges

The Project may choose to designate derivative instruments as hedges and apply hedge accounting if there is an economic relationship between the hedged item and the hedging instrument; the effect of credit risk does not dominate the value changes that result from that economic relationship; and the hedge ratio of the hedging relationship is the same as that resulting from the quantity of the hedged item that the Project actually hedges and the quantity of the hedging instrument that the entity actually uses to hedge that quantity of hedged item. The Project formally documents all hedges and the related risk management objectives at the inception of the hedge. Derivative instruments that have been designated and qualify for hedge accounting are classified as either cash flow or fair value hedges.

The effective portion of the gain or loss on a cash flow hedging instrument is recognized directly in other comprehensive income, while any ineffective portion is recognized immediately in the Combined Statement of (Loss) Profit and Comprehensive (Loss) Income for the period in other expense. Amounts recognized in other comprehensive income are transferred to the Combined Statement of (Loss) Profit and Comprehensive (Loss) Income for the period when the hedged transaction affects profit or loss, such as when the hedged financial income or financial expense is recognized or when a forecast sale occurs.

The Project does not hold any fair value hedges.

3. SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUMPTIONS

The preparation of the annual audited combined 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 differ materially 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.

LOWER CHURCHILL PROJECT COMPANIES

NOTES TO COMBINED FINANCIAL STATEMENTS

3.1 Use of Judgment

(i) Property, Plant and Equipment

The Project's accounting policy relating to property, plant and equipment is described in Note 2.5. In applying this policy, judgment is used in determining whether certain costs are additions to the carrying amount of the property, plant and equipment as opposed to repairs and maintenance. If an asset has been developed, judgment is required to identify the point at which the asset is capable of being used as intended and to identify the directly attributable borrowing costs to be included in the carrying value of the development asset. Judgment is also used in determining the appropriate componentization structure for the Project's, plant and equipment.

(ii) Functional currency

Functional currency was determined by evaluating the primary economic environment in which the Project operates. As the Project enters into transactions in multiple currencies, judgment is used in determining the functional currency. Management considered factors regarding currency of sales, costs incurred, and operating and financing activities and determined the functional currency to be CAD.

(iii) Consolidation

Management applies its judgment when determining whether to consolidate structured entities in accordance with the criteria outlined in IFRS 10.

(iv) Leases

Definition of a lease

At inception of a contract, the Project assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Project assesses whether the contract involves the use of an identified asset, the Project has the right to obtain substantially all of the economic benefits from use of the asset throughout the period of use and the Project has the right to direct the use of the asset.

Lease extension and termination options

In determining the lease term, the Project considers all facts and circumstances that create an economic incentive to exercise an extension option, or not to exercise a termination option. The assessment is reviewed if a significant event or a significant change in circumstances occurs within its control. The assessment requires the consideration of facts and circumstances such as contractual terms and conditions for option periods, significant leasehold improvements undertaken, costs to terminate the lease, the importance of the asset to the lessee's operations and past practice.

3.2 Use of Estimates

(i) Property, Plant and Equipment

Amounts recorded for depreciation are based on the useful lives of the Project's assets. The useful lives of property, plant and equipment are determined by Management's best estimate of the service lives of these assets and are reviewed on an annual basis. Changes to these lives could materially effect the amount of depreciation recorded.

(ii) Intangible Assets

Amounts recorded for amortization are based on the useful lives of the Project's assets. These useful lives are Management's best estimate of the service lives of these assets and are reviewed on an annual basis. Changes to these lives could materially affect the amount of amortization recorded.

(iii) Class B Limited Partnership Units

The Project determines the fair value of the Class B limited partnership units at each financial reporting date. These units represent Emera Newfoundland and Labrador Island Link Inc. (Emera NL)'s ownership interest in the LIL. Due to the nature of the liability and lack of comparable market data, the fair value of the Class B limited partnership unit

LOWER CHURCHILL PROJECT COMPANIES

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liability is determined using the present value of future cash flows. Significant assumptions used in the determination of fair value include estimates of the amount and timing of future cash flows and the discount rate.

The process of valuing a financial liability for which no published market price exists is based on inherent uncertainties and the resulting values may differ from values that would have been used had a ready market existed for the liability. These differences could be material to the fair value of the financial liability.

(iv) Leases incremental borrowing rate

The Project uses its incremental borrowing rates in measuring its lease liabilities. The incremental borrowing rate is the rate of interest that a lessee would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The determination of the incremental borrowing rate requires the consideration of different components, all of which are to incorporate a number of important lease characteristics.

4. CURRENT AND FUTURE CHANGES IN ACCOUNTING POLICIES

The following is a list of standards/interpretations that have been issued and are effective for accounting periods commencing on January 1, 2019 or January 1, 2020, as specified.

- IFRS 16 – Leases¹
- IAS 23 – Borrowing Costs (Amendments to IAS 23)¹
- IAS 1 – Presentation of Financial Statements² and IAS 8 – Accounting Policies, Changes in Accounting Estimates and Errors² (Amendments to IAS 1 and IAS 8)

¹ Effective for annual periods beginning on or after January 1, 2019.

² Effective for annual periods beginning on or after January 1, 2020.

4.1 IFRS 16 – Leases

Effective January 1, 2019 the Project adopted *IFRS 16 – Leases* which introduces significant changes to lessee accounting by removing the distinction between operating and finance leases and requiring the recognition of a right-of-use asset and a lease liability at the lease commencement for all leases, except for short-term leases and leases of low-value assets.

The Project has applied IFRS 16 using the modified retrospective approach and therefore the comparative information has not been restated and continues to be reported under *IAS 17 – Leases and IFRIC 4 – Determining Whether an Arrangement contains a Lease*.

Impact of the new definition of a lease

The Project has not elected to apply the practical expedient available on transition to IFRS 16, not to reassess whether a contract is or contains a lease at the date of initial application.

In preparation for the first-time application of IFRS 16, the Project has carried out an implementation project which has shown that the new definition in IFRS 16 will not significantly change the scope of contracts that meet the definition of a lease for the Project.

Impact on Lessee Accounting

Former operating leases

IFRS 16 changes how the Project accounts for leases previously classified as operating leases under IAS 17, which were off-balance-sheet.

LOWER CHURCHILL PROJECT COMPANIES
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Applying IFRS 16, for all leases (except as noted below), the Project

- (a) recognizes right-of-use assets and lease liabilities in the Combined Statement of Financial Position, initially measured at the present value of future lease payments;
- (b) capitalizes depreciation of right-of-use assets and interest on lease liabilities as use of these assets is directly attributable to the construction of the LIL, LTA and MF hydroelectric facility; and
- (c) separates the total amount of cash paid into a principal portion (presented within financing activities) and interest (presented within operating activities) in the Combined Statement of Cash Flows.

For short-term leases (lease term of 12 months or less) and leases of low-value assets (such as personal computers and office furniture), the Project would normally opt to recognize a lease expense on a straight-line basis as permitted by IFRS 16. However, as the Project is still in the construction phase of its operations, the Project has capitalized the lease payments within property, plant and equipment.

Former finance leases

The main difference between IFRS 16 and IAS 17 with respect to assets formerly held under a finance lease is the measurement of residual value guarantees provided by a lessee to a lessor. The Project did not have any leases previously accounted for as finance leases under IAS 17, therefore, this change did not have an effect on its financial statements.

Impact on Lessor Accounting

IFRS 16 does not substantially change how a lessor accounts for leases. The changes to lessor accounting did not have an effect on the Project's financial statements.

Financial impact of the application of IFRS 16

On transition to IFRS 16, the Project recognized lease liabilities in relation to leases which had previously been classified as operating leases under IAS 17. These liabilities were measured at the present value of the remaining lease payments, discounted using the Project's incremental borrowing rate as of January 1, 2019. The weighted average incremental borrowing rate applied to the lease liabilities on January 1, 2019 was 2.704% - 4.566%. The associated right-of-use assets were measured at the amount equal to the corresponding lease liabilities totalling \$5.7M.

(thousands of Canadian dollars)

Operating lease commitments disclosed as at December 31, 2018	-
Additional operating lease commitments recognized under IFRS 16 as at January 1, 2019	11,815
Total operating lease commitments	11,815
Discounted using the incremental borrowing rate of 2.704% - 4.566%	7,610
Less: short-term leases recognized on a straight-line basis	(1,826)
Less: low-value leases	(89)
Lease liability recognized as at January 1, 2019	5,695

In applying IFRS 16, the Project elected to use the following practical expedients, permitted by the standard:

- a) accounting for operating leases with a remaining lease term of less than 12 months at January 1, 2019 as short-term leases;
- b) the exclusion of initial direct costs for the measurement of the right-of-use asset at the date of initial application; and
- c) the use of hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

LOWER CHURCHILL PROJECT COMPANIES
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4.2 IAS 23 – Borrowing Costs (Amendments to IAS 23)

The amendments clarify that an entity treats as part of general borrowings any borrowing originally made to develop a qualifying asset when substantially all of the activities necessary to prepare that asset for its intended use or sale are complete. The application of these amendments to IAS 23 did not have a material impact on the Project's annual audited combined financial statements.

4.3 IAS 1 - Presentation of Financial Statements and IAS 8 – Accounting Policies, Changes in Accounting Estimates and Errors (Amendments to IAS 1 and IAS 8)

The IASB issued amendments to IAS 1 and IAS 8 to align the definition of 'material' across the standards and to clarify certain aspects of the definition and to include the concept of 'obscuring information'. The amendments are intended to improve the understanding of the existing requirements rather than to significantly impact the Project's materiality judgments.

5. INVESTMENTS

<i>As at December 31 (thousands of Canadian dollars)</i>	Year of Maturity	2019	2018
Two \$75.0 million Floating Rate Deposit Notes, with interest paid at the one-month Canadian Dollar Offered Rate (CDOR) plus 0.20%.	2019	-	150,000
\$182.9 million Amortizing Floating Rate Deposit Note, with interest paid at the one-month CDOR plus 0.20%.	2019	-	7,631
\$483.8 million Amortizing Floating Rate Deposit Note, with interest paid at the one-month CDOR plus 0.20%.	2019	-	46,923
\$548.6 million Amortizing Fixed Rate Deposit Note, with interest paid at a rate of 1.644% per annum	2019	-	22,892
\$725.7 million Amortizing Fixed Rate Deposit Note, with interest paid at a rate of 1.679% per annum.	2019	-	70,384
Total investments, end of the year		-	297,830

6. TRADE AND OTHER RECEIVABLES

<i>As at December 31 (thousands of Canadian dollars)</i>	2019	2018
HST receivable	15,510	28,375
Interest receivable	1,250	1,475
Receivable due from related parties	1,175	31
Insurance receivable	480	6,750
Letters of credit	-	184,111
	18,415	220,742

LOWER CHURCHILL PROJECT COMPANIES
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7. ADVANCES

Advances consist of deposits paid to contractors on long-term construction contracts in relation to the MF hydroelectric facility and the LIL. Advances are secured by a letter of credit from a Canadian Schedule 1 Chartered Bank or a vendor performance bond. The bond is underwritten by three sureties with Standard and Poor's ratings of A or better.

<i>As at December 31 (thousands of Canadian dollars)</i>	2019	2018
Total advances	24,899	25,923
Less: current portion	24,899	25,028
Total long-term advances	-	895

8. PROPERTY, PLANT AND EQUIPMENT

<i>(thousands of Canadian dollars)</i>	Project Support Assets	Construction in Progress	Other	Total
Cost				
Balance at January 1, 2018	216,621	8,873,885	-	9,090,506
Additions	25	1,124,802	-	1,124,827
Other adjustments	(2)	-	-	(2)
Balance at December 31, 2018	216,644	9,998,687	-	10,215,331
Additions	16	963,918	2,802	966,736
Other adjustments	(2)	-	-	(2)
Disposals	(5,435)	-	-	(5,435)
Balance at December 31, 2019	211,223	10,962,605	2,802	11,176,630
Depreciation				
Balance at January 1, 2018	151,172	-	-	151,172
Depreciation	27,803	-	-	27,803
Balance at December 31, 2018	178,975	-	-	178,975
Depreciation	26,603	-	-	26,603
Disposals	(5,435)	-	-	(5,435)
Balance at December 31, 2019	200,143	-	-	200,143
Carrying value				
Balance at January 1, 2018	65,449	8,873,885	-	8,939,334
Balance at December 31, 2018	37,669	9,998,687	-	10,036,356
Balance at December 31, 2019	11,080	10,962,605	2,802	10,976,487

Capitalized Borrowing Costs

The construction of the LIL, LTA and MF hydroelectric facility is being financed, in part, through the issuance of long-term debt and contributed capital. For the year ended December 31, 2019, \$243.4 million (2018 - \$250 million) of borrowing costs were capitalized. The Project also capitalized borrowing costs associated with the Class B units of \$45.3 million (2018 - \$41.8 million) as non-cash additions to property, plant and equipment.

LOWER CHURCHILL PROJECT COMPANIES
NOTES TO COMBINED FINANCIAL STATEMENTS

9. INTANGIBLE ASSETS

<i>(thousands of Canadian dollars)</i>	Computer Software	Assets Under Development	Total
Cost			
Balance at January 1, 2018	5,198	33,182	38,380
Additions	688	1,721	2,409
Balance at December 31, 2018	5,886	34,903	40,789
Additions	497	734	1,231
Balance at December 31, 2019	6,383	35,637	42,020
Amortization			
Balance at January 1, 2018	4,843	-	4,843
Amortization	697	-	697
Balance at December 31, 2018	5,540	-	5,540
Amortization	555	-	555
Balance at December 31, 2019	6,095	-	6,095
Carrying value			
Balance at January 1, 2018	355	33,182	33,537
Balance at December 31, 2018	346	34,903	35,249
Balance at December 31, 2019	288	35,637	35,925

10. RIGHT-OF-USE ASSETS

The Project has leases for various properties, including easements, and leases for equipment rentals. The fixed period on these contracts range between 1-60 years. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The lease agreements do not impose any covenants, but leased assets may not be used as security for borrowing purposes.

Extension and termination options are included in a number of property leases and easements across the Project. These terms are used to maximize operational flexibility in terms of managing contracts. The majority of extension and termination options held are exercisable only by the Project and not by the respective lessor.

<i>(thousands of Canadian dollars)</i>	Property	Equipment	Total
Cost			
Balance at January 1, 2019	5,253	442	5,695
Balance at December 31, 2019	5,253	442	5,695
Depreciation			
Balance at January 1, 2019	-	-	-
Depreciation	1,460	93	1,553
Balance at December 31, 2019	1,460	93	1,553
Carrying value			
Balance at January 1, 2019	5,253	442	5,695
Balance at December 31, 2019	3,793	349	4,142

LOWER CHURCHILL PROJECT COMPANIES
NOTES TO COMBINED FINANCIAL STATEMENTS

11. TRADE AND OTHER PAYABLES

<i>As at December 31 (thousands of Canadian dollars)</i>	2019	2018
Trade payables	166,652	245,598
Accrued interest	30,531	30,531
Payables due to related parties	11,701	15,465
HST payable	3,811	3,568
	212,695	295,162

12. LONG-TERM DEBT

The following table represents the value of long-term debt measured at amortized cost as at December 31:

<i>(thousands of Canadian dollars)</i>	Face Value	Coupon Rate %	Year of Issue	Year of Maturity	2019	2018
LIL LP						
Tranche A	725,000	3.76	2013	2033	725,210	725,226
Tranche B	600,000	3.86	2013	2045	600,093	600,096
Tranche C	1,075,000	3.85	2013	2053	1,075,192	1,075,197
Tranche 1-10	105,000	1.14-1.75	2017	2020-2025	105,014	105,020
Tranche 11-20	105,000	1.84-2.37	2017	2025-2030	105,025	105,028
Tranche 21-30	105,000	2.41-2.64	2017	2030-2035	105,049	105,053
Tranche 31-40	105,000	2.66-2.80	2017	2035-2040	105,101	105,107
Tranche 41-50	105,000	2.81-2.86	2017	2040-2045	105,106	105,111
Tranche 51-60	105,000	2.84-2.86	2017	2045-2050	105,135	105,140
Tranche 61-70	105,000	2.85	2017	2050-2055	105,196	105,202
Tranche 71-74	315,000	2.85	2017	2055-2057	315,632	315,648
Muskrat Falls/Labrador Transco						
Tranche A	650,000	3.63	2013	2029	650,142	650,158
Tranche B	675,000	3.83	2013	2037	675,081	675,084
Tranche C	1,275,000	3.86	2013	2048	1,275,211	1,275,219
Tranche 1-10	204,763	1.14-1.75	2017	2020-2025	204,792	204,801
Tranche 11-20	224,283	1.84-2.37	2017	2025-2030	224,336	224,343
Tranche 21-30	252,595	2.41-2.64	2017	2030-2035	252,712	252,721
Tranche 31-40	288,185	2.66-2.80	2017	2035-2040	288,465	288,481
Tranche 41-50	331,037	2.81-2.86	2017	2040-2045	331,370	331,384
Tranche 51-60	381,084	2.84-2.86	2017	2045-2050	381,579	381,596
Tranche 61-64	168,053	2.85	2017	2050-2052	168,358	168,368
Total	7,900,000				7,903,799	7,903,983
Less: maturities of debt within one year					(30,411)	-
					7,873,388	7,903,983

LOWER CHURCHILL PROJECT COMPANIES

NOTES TO COMBINED FINANCIAL STATEMENTS

On November 29, 2013, the IT entered into the IT Project Finance Agreement (IT PFA) with the LIL Funding Trust, LIL LP, LIL Opco and the Collateral Agent. Under the terms and conditions of the IT PFA, the LIL Funding Trust agreed to provide a credit facility in the amount of \$2.4 billion available in three tranches (Tranches A, B and C) to the IT, which itself proceeded to on-lend this amount to LIL LP under the terms of the LIL PFA. On December 13, 2013, all three tranches of the construction facility were drawn down by way of a single advance to the IT of \$2.4 billion to an account administered by the Collateral Agent. On May 10, 2017, the IT entered into second amendments to the IT PFA and the LIL PFA. Under the terms and conditions of the second amended IT PFA, the LIL Funding Trust agreed to provide an additional credit facility in the amount of \$1.05 billion to the IT. These facilities, available in a series of 74 bonds with maturities of every six months beginning in December 2020, were fully drawn down by the IT on May 25, 2017 by way of a single advance to an account administered by a Collateral Agent. LIL LP draws funds from this account on a monthly basis in accordance with procedures set out in the LIL PFA. As at December 31, 2019, the \$2.4 billion construction facility was fully utilized by LIL LP (2018 - \$2.4 billion) and \$1.0 billion of the second construction facility was utilized by LIL LP (2018 - \$0.7 billion).

The purpose of the LIL Funding Trust is to issue long-term debentures to the public and to on-lend the proceeds to the IT, which in turn on-lends funds to LIL LP. The financing of the LIL Funding Trust benefits from a direct, absolute, unconditional and irrevocable guarantee from the Government of Canada, and thereby carries its full faith and credit (AAA rating or equivalent). Included in the terms of the guarantee, LIL LP agreed to pay an annual fee starting in May 2018 equal to 0.5% of the average balance outstanding on Tranches 1 through 74 for the prior twelve months.

On November 29, 2013, Muskrat Falls and Labrador Transco entered into the MF/LTA PFA with the MF/LTA Funding Trust and the Collateral Agent. Under the terms and conditions of the MF/LTA PFA, the MF/LTA Funding Trust agreed to provide a credit facility in the amount of \$2.6 billion available in three tranches (Tranches A, B and C). On December 13, 2013, all three tranches of the construction facility were drawn down by way of a single advance to an account administered by a Collateral Agent. On May 10, 2017, Muskrat Falls and Labrador Transco entered into 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 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. Muskrat Falls and Labrador Transco draw funds from this account on a monthly basis in accordance with procedures set out in the MF/LTA PFA. As of December 31, 2019, the \$2.6 billion construction facility was fully utilized by Muskrat Falls and Labrador Transco (2018 - \$2.6 billion) and \$1.7 billion of the second construction facility was utilized by Muskrat Falls and Labrador Transco (2018 - \$1.4 billion).

The purpose of the MF/LTA Funding Trust is to issue long-term debentures to the public 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. 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 December 31, 2019, Muskrat Falls' cumulative portion of actual debt drawn was 83% (2018 – 83%) and Labrador Transco's cumulative portion of actual debt drawn was 17% (2018 – 17%).

The financing of the MF/LTA Funding Trust benefits from a direct, absolute, unconditional and irrevocable guarantee from the Government of Canada, and thereby carries its full faith and credit (AAA rating or equivalent). Included in the terms of the guarantee, Muskrat Falls and Labrador Transco agreed to pay an annual 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.

The role of the Collateral Agent is to act on behalf of the lending parties, including the LIL Funding Trust, the MF/LTA 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, LIL LP, Muskrat Falls and Labrador Transco have granted to the Collateral Agent first ranking liens on all present and future assets. Sinking funds are required to be set up for the Tranche A, B and C debentures and are to be held in a sinking fund account under the control of the Collateral Agent.

LOWER CHURCHILL PROJECT COMPANIES
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Sinking fund instalments due for the next five years are as follows:

<i>(thousands of Canadian dollars)</i>	2020	2021	2022	2023	2024
Sinking fund instalments	63,996	127,991	127,991	127,991	127,991

13. LEASE LIABILITIES

<i>As at December 31 (thousands of Canadian dollars)</i>	2019
Maturity analysis – contractual undiscounted cash flows	
Less than one year	1,531
One to five years	802
More than five years	5,937
Total undiscounted lease liabilities	8,270
Lease liabilities included in the Statement of Financial Position	
Current lease liabilities	1,388
Non-current lease liabilities	2,827
Total lease liabilities	4,215

Interest on lease liabilities, expenses relating to short-term and low-value leases and variable lease payments not included in the measurement of leases are capitalized within, property, plant and equipment when permitted by IAS 16.

The total cash outflow for leases for the year ended December 31, 2019 is \$3.3 million.

14. DEFERRED REVENUE

LIL Opco has the option to prepay rent in accordance with the LIL Lease. For the year ended December 31, 2019, LIL Opco had a prepayment balance of \$52.3 million (2018 - \$36.5 million) to the Partnership. The Partnership has recognized these prepayments as deferred revenue which will be amortized to income once the LIL is in-service.

15. LIMITED PARTNERSHIP UNITS

Debt and equity instruments issued by LIL Holdco are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

The Class B limited partnership units represent Emera NL's ownership interest in the LIL LP. As described in the LIL Limited Partnership Agreement, these units have certain rights and obligations, including mandatory distributions, that indicate that the substance of the units represent a financial liability and are measured at amortized cost using the effective interest method.

Class B Limited Partnership Units

<i>As at December 31 (thousands of Canadian dollars)</i>	Units	2019	Units	2018
Class B limited partnership units, beginning of year	25	533,058	25	491,298
Accrued interest	-	45,310	-	41,760
Class B limited partnership units, end of year	25	578,368	25	533,058

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16. SHAREHOLDER'S EQUITY

Share Capital

<i>As at December 31 (thousands of Canadian dollars)</i>	2019	2018
Common shares without nominal or par value		
Authorized - unlimited		
Issued - fully paid and outstanding - 400	4	4

17. NET FINANCE EXPENSE (INCOME)

<i>For the year ended December 31 (thousands of Canadian dollars)</i>	2019	2018
Finance income		
Interest on investments	793	15,737
Other interest income	29,312	17,712
	30,105	33,449
Finance expense		
Interest and fees on long-term debt	279,383	279,371
Interest on lease liabilities	118	-
Interest on Class B limited partnership units	45,310	41,760
Bank fees and other interest expense	39	31
	324,850	321,162
Interest capitalized during construction	(288,703)	(291,843)
	36,147	29,319
Net finance expense (income)	6,042	(4,130)

18. OPERATING COSTS

<i>For the year ended December 31 (thousands of Canadian dollars)</i>	2019	2018
Salaries and benefits expense	4,556	1,290
Professional services	1,285	230
Training	655	973
Maintenance and materials	581	-
Cost recoveries and other	519	475
Travel and transportation	264	-
Donations and community involvement	14	156
	7,874	3,124

19. OTHER EXPENSE

<i>For the year ended December 31 (thousands of Canadian dollars)</i>	2019	2018
Cash flow hedge amortization	326	-
Gain on disposal of property plant and equipment	(233)	-
Realized foreign exchange (gain) loss	(8)	126
Unrealized foreign exchange (gain) loss	(26)	62
Other expense	59	188

LOWER CHURCHILL PROJECT COMPANIES
NOTES TO COMBINED FINANCIAL STATEMENTS

20. DISTRIBUTION OF INCOME

In accordance with the LIL Declaration of Trust, the Project Trust elects to make an annual distribution of income to the beneficiaries of the Trust, which is designated as a registered charity in Nova Scotia.

21. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

21.1 Fair Value

The estimated fair values of financial instruments as at December 31, 2019 and 2018 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 the Project might receive or incur in actual market transactions.

As a significant number of the Project'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 the Project 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).

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 Project 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 years ended December 31, 2019 and 2018.

	Level	Carrying Value	Fair Value	Carrying Value	Fair Value
		2019		2018	
<i>As at December 31 (thousands of Canadian dollars)</i>					
Financial assets					
Investments	2	-	-	297,830	297,760
Financial liabilities					
Long-term debt including amount due within one year	2	7,903,799	9,333,816	7,903,983	8,608,064
Class B limited partnership units	3	578,368	578,368	533,058	533,058

The fair values of cash, restricted cash, trade and other receivables, advances, 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

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interest rate yield curves.

The Class B limited partnership units are carried at amortized cost, calculated using the effective interest method, which approximates fair value. The effective interest rate of 8.5% (2018 - 8.5%) is defined in the Newfoundland and Labrador Development Agreement as Emera NL's rate of return on equity, and is equal to the rate approved by the Newfoundland and Labrador Board of Commissioners of Public Utilities for privately-owned regulated electrical utilities. Due to the unobservable nature of the effective interest rate and resulting discounted cash flows associated with the units, the instruments have been classified as Level 3.

The table below sets forth a summary of changes in fair value of the Project's Level 3 financial liabilities given a one percent change in the discount rate while holding other variables constant:

<i>(thousands of Canadian dollars)</i>	1% increase in discount rate	1% decrease in discount rate
Class B limited partnership units	(23,310)	22,515

21.2 Risk Management

The Project is exposed to certain credit, liquidity and market price 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 Project's expected future cash flows.

Credit Risk

The Project's expected future cash flows are exposed to credit risk through financing activities, primarily due to the potential for non-performance by counterparties to its financial instruments. Credit risk on cash, restricted cash and investments is minimal, as the Project's deposits are held by Canadian Schedule 1 Chartered Banks with ratings of A, 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 Combined Statement of Financial Position at the reporting date.

Liquidity Risk

The Project 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 cash, restricted cash on hand and partnership and shareholder contributions. Muskrat Falls, Labrador Transco and LIL LP can access the funds drawn down from the Muskrat/LTA and LIL construction facilities, partnership contributions and shareholder contributions for the payment of construction costs as well as interest payments.

The following are the contractual maturities of the Project's financial liabilities, including principal, sinking funds and interest as at December 31, 2019:

<i>(thousands of Canadian dollars)</i>	< 1 Year	1-3 Years	3-5 Years	> 5 Years	Total
Trade and other payables	212,695	-	-	-	212,695
Long-term debt (including interest and sinking fund)	359,248	906,408	905,213	11,848,151	14,019,020
Unit B partnership units	9,857	153,711	152,857	3,190,687	3,507,112
	581,800	1,060,119	1,058,070	15,038,838	17,738,827

Market Risk

In the course of carrying out its operating, financing and investing activities, the Project is exposed to possible market price movements that could impact expected future cash flow and the carrying value of certain financial assets and liabilities.

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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.

In May 2017, Muskrat Falls and Labrador Transco entered into three bond forward contracts of \$1.8 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 of \$65.9 million was recorded in other comprehensive income (loss) with the ineffective portion of \$1.1 million 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 the Muskrat Falls and Labrador Transco assets are ready for their intended use. At that point, 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 in 2019 including the previous cash flow hedge initiated in December 2013 was \$3.7 million (2018 - \$3.7 million).

Foreign Currency and Commodity Exposure

The Project does not hold any financial instruments whose value would vary due to changes in a commodity price or whose value would materially vary due to fluctuations in foreign currency exchange rates. Cash flow exposure to 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.

22. RELATED PARTY TRANSACTIONS

The Project 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 the Project transacts are as follows:

Related Party	Relationship
Nalcor	100% shareholder of LIL Holdco, Labrador Transco, LCMC, LIL Opco, Labrador-Island Link General Partner and Muskrat Falls Limited Partner holding 25 Class B limited partnership units of LIL LP
Emera NL	Limited Partner holding 25 Class B limited partnership units of LIL LP
Labrador-Island Link General Partner	General partner of LIL LP, wholly-owned subsidiary of Nalcor
LIL Opco	Wholly-owned subsidiary of Nalcor
Hydro	Wholly-owned subsidiary of Nalcor
LIL Funding Trust	Party to the IT PFA
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 December 31, 2019, the Project has related party payables totaling \$11.7 million (2018 - \$15.5 million) with Nalcor and Hydro and related party receivables totalling \$1.2 million (2018 - \$31 thousand) with Hydro, Nalcor and LIL Opco. These payables consist of various intercompany operating and construction costs.
- (b) The Project has a \$50.0 million (2018 - \$50.0 million) unsecured revolving credit facility with Nalcor. As at December 31, 2019, there was no balance outstanding (2018 - \$nil) on this credit facility.
- (c) For the year ended December 31, 2019, LIL LP had incurred costs of \$0.7 million (2018 - \$1.7 million) related to assets under development which LIL LP controls the right to collect costs through the LIL Lease and TFA with LIL Opco and Hydro.

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- (d) For the year ended December 31, 2019, the Project has received contributions from Nalcor totaling \$495.7 million (2018 - \$529.4 million).
- (e) For the year ended December 31, 2019, LIL Opco prepaid rent to the Partnership in the amount of \$15.8 million (2018 - \$11.6 million).
- (f) For the year ended December 31, 2019, LCMC had revenue of \$0.4 million (2018 - \$0.4 million) for providing project development and management functions for Muskrat Falls, Labrador Transco and LIL LP.
- (g) For the year ended December 31, 2019, LCMC was charged \$20.9 million (2018 - \$29.7 million) by Nalcor and Hydro related to intercompany salary costs, administrative services and power purchases for the Lower Churchill Project. LCMC subsequently passes on these costs to Muskrat Falls, Labrador Transco, and LIL LP as part of the project development and management functions LCMC provides to these companies.

23. COMMITMENTS AND CONTINGENCIES

- (a) The Partnership is required to make mandatory distributions in accordance with the Partnership Agreement. The amount of periodic distributions will be determined by the General Partner and will commence following commissioning of the LIL.
- (b) As part of the LIL PFA, LIL LP has pledged its current and future assets as security to the Collateral Agent. Under the terms and conditions of the IT PFA, LIL LP has also provided a guarantee of the IT's payment obligations to the Collateral Agent for the benefit of the LIL Funding Trust. LIL Holdco has pledged the escrow account, where pre-funded equity contributions have been deposited, as security to the Collateral Agent.
- (c) Under the terms and conditions of the Partnership Agreement, LIL Holdco had committed to fund its share of the capital expenditures of the LIL.
- (d) LIL LP has entered into the LIL Lease and the TFA with LIL Opco and Hydro, whereby LIL LP has committed to design and construct the LIL and LIL Opco will operate and maintain the LIL at commissioning and provide such other services as agreed to ensure safe and reliable transmission of electricity. During 2018, LIL LP also entered into the Interim Transmission Funding Agreement with Hydro, whereby LIL LP will operate and maintain the LIL pre-commissioning during the pre-full commissioning interim use period and provide such services as agreed to ensure safe and reliable transmission of electricity.
- (e) Muskrat Falls and Labrador Transco have entered into the GIA with Hydro, and Muskrat Falls has entered into the PPA with Hydro for an expected term of 55 years, whereby Muskrat Falls and Labrador Transco have committed to design, construct, operate and maintain the Muskrat Falls hydroelectric facility and LTA, and provide such other services as agreed to ensure safe and reliable transmission of electricity. During 2018, Labrador Transco also entered into the Interim Transmission Funding Agreement with Hydro, whereby Labrador Transco will operate and maintain the LTA during the pre-full commissioning interim use period and provide such services as agreed to ensure safe and reliable transmission of electricity.
- (f) In July 2012, Nalcor entered into the Energy and Capacity Agreement with Emera NL providing for the sale and delivery of the Nova Scotia Block, being 0.986 TWh of energy annually for a term of 35 years and supplemental energy over the initial five years of the term. In October 2015 Nalcor assigned this agreement to Muskrat Falls. As a result of this assignment, Nalcor and Muskrat Falls are jointly liable for the delivery of the Nova Scotia Block to Emera.
- (g) As part of the MF/LTA PFA, Labrador Transco and Muskrat Falls have pledged their present and future assets as security to the Collateral Agent.

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- (h) The Project 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 the Project's exposure to such claims and litigation, to the extent not covered by insurance policies or otherwise provided for, will not materially affect its financial position.
- (i) Outstanding commitments for capital projects total approximately \$165.8 million as at December 31, 2019 (2018 - \$356.2 million). Pre-funded equity requirements associated with the Project Finance Agreements are \$nil (2018 - \$505.4 million). Pre-funded equity is used to fund capital and borrowing costs.

24. CAPITAL MANAGEMENT

Capital includes partner capital, share capital, shareholder contributions, deficit and long-term debt. The Project'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 LIL, the LTA and the MF hydroelectric facility. During this time, it is expected that proceeds from the construction facilities and shareholder contributions will be sufficient to fund the development of the assets. The Province of Newfoundland and Labrador has provided guarantees of equity support in relation to the construction of the Project. These guarantees, together with the proceeds from long-term debt, will ensure sufficient funds are available to finance construction.

25. SUPPLEMENTARY CASH FLOW INFORMATION

<i>For the year ended December 31 (thousands of Canadian dollars)</i>	2019	2018
Trade and other receivables	203,565	(115,174)
Prepayments	(719)	3,733
Trade and other payables	(82,467)	(62,669)
Changes in non-cash working capital balances	120,379	(174,110)
Related to:		
Operating activities	(14,307)	1,420
Investing activities	134,686	(175,530)
	120,379	(174,110)

26. SUBSEQUENT EVENT

On February 10, 2020, the provincial and federal governments announced a plan to negotiate a financial restructuring of the Lower Churchill Project, including a change to the Muskrat Falls/Labrador Transmission Assets revenue model and the deferral of sinking fund payments and Cost Overrun Escrow Account payments, if required. A formal agreement between both levels of government is anticipated by project commissioning. As further information regarding the financial restructure becomes known, management will continue to assess the associated financial reporting impacts.