

2017

ANNUAL REPORT



**OUR
PEOPLE**

**OUR
PLACE**

**OUR
BUSINESS**

We are committed to developing and managing Newfoundland and Labrador's energy resources safely and responsibly.



04	2017 Achievements
07	Corporate Profile
08	Message From the Chair
10	Message From the CEO
12	Safety

Business Excellence

14	Muskrat Falls Project
20	Hydro
26	Oil and Gas
32	Bull Arm
36	Energy Marketing
38	Churchill Falls
42	Community
45	People
46	Environment and Sustainability
48	Operating Statistics
49	Financial Statistics
50	Executive, Directors and Officers
52	Corporate Governance

Appendix 1

Management's Discussion and Analysis

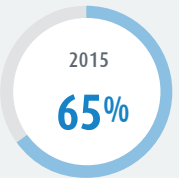
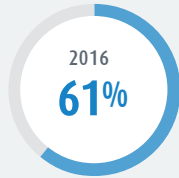
Appendix 2

Consolidated Financial Statements -
December 31, 2017

2017

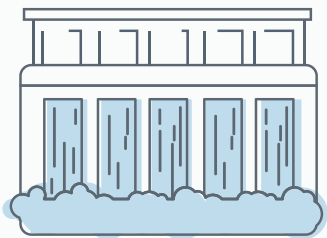
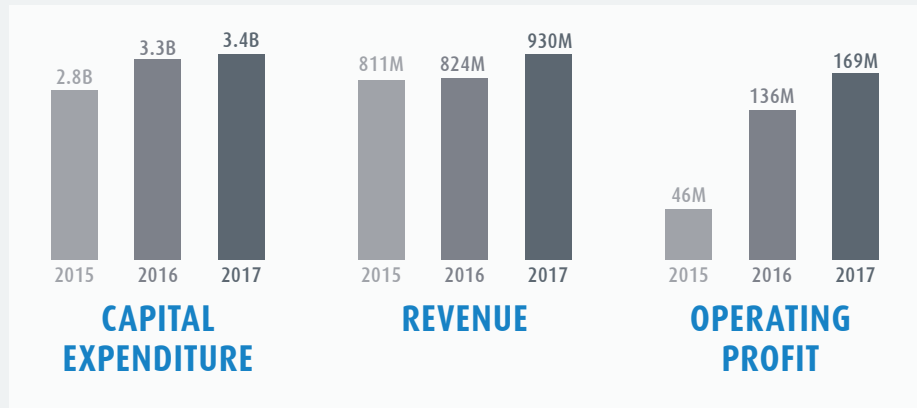
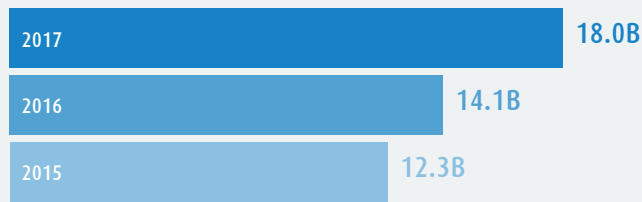
ACHIEVEMENTS

FINANCIAL

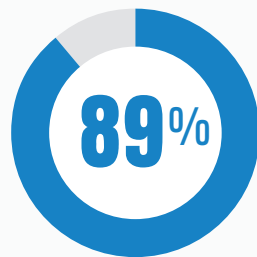


DEBT TO CAPITAL

TOTAL ASSETS

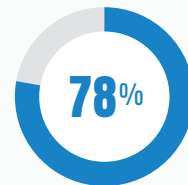


MUSKRAT FALLS

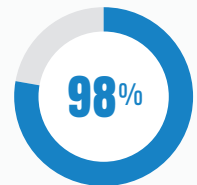


TOTAL PROJECT CONSTRUCTION

COMPLETE



GENERATION



LABRADOR-ISLAND TRANSMISSION LINK

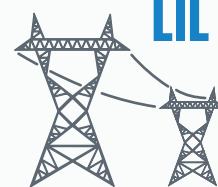


8,200 SKILLED

Newfoundlanders and Labradorians employed

TWO OF THE THREE DAMS

required to create the Muskrat Falls reservoir completed



LIL STRINGING

completed with **2,250 KM** of wire strung

*Labrador-Island Transmission Link



HYDRO

✓ To enhance reliability more than **150 PROJECTS** completed

✓ close to **5,000 ACTIVITIES** carried out on equipment and facilities

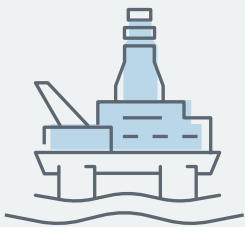
85% satisfaction rate among commercial customers



Construction of new transmission line from Bay d'Espoir to the Avalon Peninsula completed and placed in service

NEW PROGRAM

for customers with critical needs who have greater reliance on electrical service launched



OIL & GAS



Construction of the **WEST WHITE ROSE** started



\$2.55 BILLION in operator work commitments over the last three years and seven new entrants



Hebron produced **FIRST OIL**

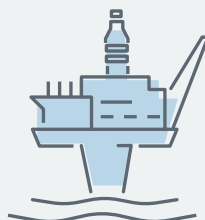
NOVEMBER 27



Over **170,000 LINE KILOMETRES** of 2D seismic data collected since 2011



BULL ARM



HEBRON PLATFORM towed to field

New tenant opportunities to maximize the value of the site



SAFETY



9% REDUCTION

in recordable injuries over previous year

ZERO LOST TIME INJURIES

maintained in several areas

ENVIRONMENT



Environmental Management System

TARGETS COMPLETED

3 CONSECUTIVE YEARS

COMMUNITY

DONATED OVER \$600,000

to more than

20 ORGANIZATIONS throughout Newfoundland and Labrador

PEOPLE

CONTINUED TO BUILD

a diverse and inclusive workforce



ENERGY MARKETING



99%

of available recapture energy delivered to market

**THE MUSKRAT FALLS
GENERATING FACILITY,
ONCE COMPLETED,
WILL BE THE 2ND LARGEST
HYDRO PLANT IN
ATLANTIC CANADA.**

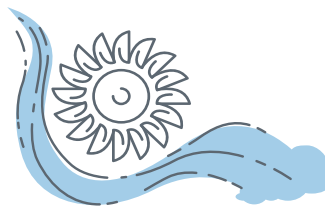


CORPORATE PROFILE



NEWFOUNDLAND AND LABRADOR HYDRO

Hydro manages Newfoundland and Labrador’s electricity system. Through our generation, transmission and distribution operations, we’re committed to meeting the needs of our customers and providing residents, businesses and communities across the province with safe, reliable power.



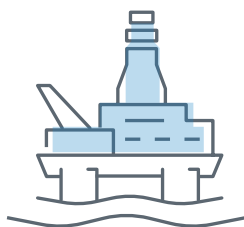
CHURCHILL FALLS

One of the world’s largest underground hydroelectric powerhouses with a rated capacity of 5,428 megawatts, Churchill Falls provides clean, renewable electricity to millions of consumers across North America.



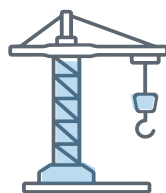
LOWER CHURCHILL PROJECT

The Lower Churchill River is one of the most attractive hydroelectric resources in North America. Muskrat Falls and Gull Island have a combined capacity of more than 3,000 megawatts. The development of the Muskrat Falls Project includes construction of an 824 megawatt hydroelectric dam and more than 1,600 kilometres of transmission lines that will provide long-term, clean, renewable energy.



OIL AND GAS

Nalcor is a partner in the development of the Newfoundland and Labrador offshore including the Hebron oil field, White Rose Growth Project and Hibernia Southern Extension. With a multi-year exploration strategy, Nalcor is systematically finding and quantifying the province’s oil and gas resource potential to facilitate new exploration investments.



BULL ARM

The Bull Arm Fabrication site is Atlantic Canada’s largest fabrication site. The site’s magnitude, diversity of infrastructure and strategic location offer a unique opportunity for fabrication, concrete construction, deep water commissioning, marine operations and supply servicing.



ENERGY MARKETING

Nalcor actively trades and sells the province’s surplus power to customers in external energy markets. The Energy Marketing portfolio includes Churchill Falls recall power and long-term transmission agreements through Québec.

MESSAGE FROM THE CHAIR

Brendan Paddick, Chair, Board of Directors



As Chair of the Board of Directors for Nalcor Energy, I am pleased to present the 2017 annual report. A company's annual report offers the opportunity to reflect on its achievements and shortcomings and to set a plan for its future goals. The past year was not without its challenges, but we continued to move forward to support growth and sustainability in managing our Province's energy resources.

Last year, shortly after our collective appointment, your board committed to ensuring that sound governance would guide all of our decisions in overseeing

Nalcor and its many subsidiary companies. This commitment included (i) setting a clear **vision** (including establishing objectives, goals, strategies and plans), (ii) enforcing strong **financial** controls and cost discipline, (iii) ensuring forward-looking **human resource** assessment and capacity-building, (iv) **managing enterprise risk**, and (v) acting as brand ambassadors that shape a progressive and high-performing **corporate culture**.

It is my belief that we made significant positive progress on all of these fronts in large part due to the leadership and commitment shown by our CEO, our senior management team, and our dedicated and experienced employees. The diversity of our board gives us a wealth of knowledge around the table, which better informs our decision-making and guides us in steering the company continuously towards optimal performance.

Our commitment to open and transparent governance ensures our work here is sound, focused and fiscally responsible. Last year we supported the CEO in his restructuring of certain divisions to better position Nalcor to

succeed in the critical areas of power generation and power distribution. This year we saw the positive results of that restructuring process. For the first time, we met, and in some instances, exceeded our construction targets for the Muskrat Falls Project. With the project 89 per cent complete, we are looking forward to first power coming on line in 2019.

Our work as a board in managing Nalcor is not only focused on the short term, but also on building a longer term vision for the effective and strategic stewardship of the Province's energy resources. Our responsibility to the people of Newfoundland and Labrador is to lead the way in ensuring your interests are our priorities.

With the construction aspect of Muskrat Falls under better control and significantly de-risked, the board and management turned its collective attention to identifying short and long term opportunities for rate mitigation. This focus is grounded on the principle that our customers should reap the maximum benefit from our energy developments, including increased capacity and enhanced reliability, at regionally competitive rates.

Underpinning that vision is our unwavering commitment to safety, environmental integrity, and community engagement and partnership. Every day across the entire province, our employees work hard to bring their best to their jobs, to ensure the safety of their coworkers, and to focus on excellence in providing reliable, quality service to our communities and industries.

On behalf of all of my fellow directors, thank you again for placing your trust in us. We collectively look forward to another year marked by successful milestones and accomplishments.

Brendan Paddick
Chair, Board of Directors



**THROUGH
STRATEGIC
INVESTMENTS IN
OUR ELECTRICITY
INFRASTRUCTURE,
WE ARE IMPROVING
RELIABILITY FOR
CUSTOMERS.**

MESSAGE FROM THE CEO

Stan Marshall, President and CEO



As we move closer to first power in 2019, we will focus on finding all reasonable measures to manage costs and minimize the impact on electricity rates for our customers.

Our company's mandate is to develop and manage the energy resources of Newfoundland and Labrador for the benefit of the people of the province.

In 2016, we separated the construction of the generation and transmission components of the Muskrat Falls Project to bring greater focus to each. In 2017, we achieved significant progress on both. Due to the hard work of more than 8,200 skilled Newfoundlanders and Labradorians and more than a thousand workers from outside our province, construction of the Muskrat Falls project reached 89 per cent completion.

Last year the Muskrat Falls generation project enclosed the powerhouse and intake structures and started the assembly and installation of the four generating units in the powerhouse. We also finished the South and North Spur dams, two of the three dams required to create the Muskrat Falls reservoir. As well, we made significant progress on the North dam.

In 2017, we completed construction of the Labrador-Island Transmission Link, an important milestone that marked the completion of all

transmission construction. We began energizing parts of the new transmission system, and successfully integrated the Soldiers Pond AC switchyard into Newfoundland and Labrador Hydro's electrical grid; bringing us closer to delivering energy from Labrador to the island for the first time.

We invested time and resources into cultivating stronger relationships with our Innu Nation partner, and all Indigenous groups including the NunatuKavut Community Council (NCC) and the Nunatsiavut Government. We have a manager of Indigenous Affairs in Labrador. We signed a Community Development Agreement with NCC, bringing long-term benefits to NunatuKavut communities and their residents. In March, with our Muskrat Falls Project partner the Innu Nation, we celebrated one million hours worked by Innu Nation members since the start of project construction.

In 2017, Hydro built critical transmission infrastructure to increase system resiliency and improve reliability. The Bay d'Espoir-to-Avalon Peninsula transmission corridor received a substantial upgrade with a new

transmission line. With this new transmission asset, we have greatly increased capacity and reliability into the Avalon.

Our Oil and Gas team continued its offshore exploration activity and we saw significant global investment in the province's offshore oil and gas industry. After five years of construction, the Hebron platform was towed to field in June and produced its first oil in November. Construction also started on the West White Rose project in late 2017, with first oil expected in late 2022. In October, Bull Arm released a Request for Proposals for a new tenant for the site that will maximize the benefit of this asset for the people of our province.

Our company performed strongly on the financial front, with year-over-year increases in revenues and profit for 2017. Our asset base grew to \$18.0 billion in 2017 from \$14.1 billion in 2016. We also obtained an expanded loan guarantee from the Government of Canada, which allowed

us to successfully raise an additional \$2.9 billion in debt financing for the Muskrat Falls Project. This additional financing reduced the equity required from the provincial government and will also reduce the projected residential customer electricity rates.

The achievements we see today are possible thanks to our employees and staff. Our dedicated, knowledgeable workforce is committed to generating and delivering a safe, reliable supply of electricity for families, communities and industries throughout Newfoundland and Labrador. I am proud of the work they do, their commitment to safety, and the concern they show for each other and the environment.

As we look forward to 2018, my commitment and focus is to build on the great year of success we saw in 2017 and ensure a safe and strong finish for the Muskrat Falls Project. We will keep working on integrating the Muskrat Falls assets into the electricity system. We will focus on taking all reasonable measures to manage project

costs and pursue ways to reduce the electricity rate impact to customers. We are on target to bring power from Churchill Falls to the island by mid-2018. As communicated by the province on March 26, 2017, our Oil and Gas subsidiary will be established as a stand-alone Crown corporation. We will support our Oil and Gas colleagues and business during this transition.

I look forward to continuing to work with the Board of Directors, our exceptional team of employees across the company, and our many diverse partners in the industry and community in the year ahead.



Stan Marshall
President and CEO

Safety

FAMILIES RELY ON US TO BE SAFE

Our clear and focused safety vision inspires and supports our safety-first work culture.

World-class safety is not defined by achieving our leading and lagging metrics in a single year. It's about sustaining excellent safety performance year after year. It means always striving to be better. Our clear and focused safety vision inspires and supports our safety-focused work culture. It guides us in everything we do. Our primary goals of achieving world-class safety standards

and supporting an injury-free workplace are ones which are embraced by every person in the organization.

STEADY IMPROVEMENT

Our efforts to meet and exceed world-class safety standards continues to move in the right direction. When we reflect on our work in this area in the last few years, we see steady improvements in our safety performance.

Our work sites are busy and they encompass many different kinds of work. Keeping safety at the forefront is critical; it requires our collective effort to ensure the work is always done safely no matter what the task or timeline. In spite of our high volume of activity, many of our work areas have sustained zero lost-time injuries over an extended period.

RENEWED COMMITMENT TO SAFETY

Our robust safety program supports and encourages our people to renew their commitment to working safely each day when they come to work.



DAYS SINCE LAST LOST TIME INJURY:



TROC: 1,732	Hydro Gen: 3,149
TRON: 1,534	TRO NS: 5,457

We are reminded of how important this commitment is when incidents happen. In June 2017, one of Hydro’s contractors lost two employees while working on the construction of the new transmission line from Bay d’Espoir to the Avalon Peninsula. This loss devastated their families, co-workers, communities, and our organization as a whole. Tragedies like this remind us we cannot become complacent when it comes to safety.

Nalcor’s safety culture encourages and relies on open reporting through the company’s Safe Workplace Observation Program (SWOP). Our employees see reporting as important; as a result, last year there was a 20 per cent increase in the number of safety observations entered into the SWOP database.

Employees recorded more than 10,000 observations in 2017 and these provide continuous learning and improvement opportunities across our operations.

A FOCUS ON PUBLIC AND CONTRACTOR SAFETY

Safety programs and communications aimed at enhancing contractor and public safety made gains in 2017. Newfoundland and Labrador Hydro continued its partnership with Newfoundland Power, the Newfoundland and Labrador Construction Safety Association and Workplace NL in an ongoing campaign promoting power line safety to the public, heavy equipment operators and contractors.

The safety of our people is our top priority; it is the measure of success that matters the most.

Over 10,000 safety observations reported - a 20% increase over 2016

9% reduction in recordable injuries over previous year, with zero recordable injuries in the last two months of the year - our busiest season

Corporate Safety Metrics show improvements over 2016 year-end metrics

KEY PERFORMANCE INDICATORS

All-injury Frequency	Lost-Time Injury Frequency	Lead/Lag Ratio
0.72	0.07	1042:1



Muskrat Falls Project

A YEAR OF SIGNIFICANT CONSTRUCTION PROGRESS



89%
OF TOTAL PROJECT
CONSTRUCTION
COMPLETE

The Muskrat Falls generating facility, once completed, will be the 2nd largest hydro plant in Atlantic Canada.

The Muskrat Falls Project reached 89% completion

The generation project reached 78% completion

The Labrador-Island Transmission Link (LIL) reached 98% completion

Two of the three dams required to create the Muskrat Falls reservoir completed

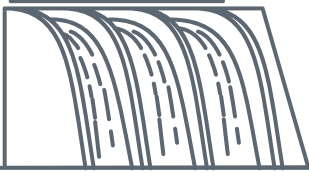
LIL stringing completed with 2,250 km of wire strung



As our largest construction project, the Muskrat Falls Project requires extensive management, oversight and coordination to ensure safe and successful completion. When the Muskrat Falls generating facility begins operation, it will be the second largest hydro plant in Atlantic Canada, behind Churchill Falls.

With the hard work of more than 8,200 skilled workers from our province, we achieved many important milestones in 2017.

The transmission project, for example, marks the first physical connection between Labrador and Newfoundland.



GENERATION

The work we completed on the generation project this year moves us closer to delivering first power in 2019.

The powerhouse, spillway and three dams are the primary components of the generating facility that span the lower Churchill River to create the reservoir, which is the source of power for the plant. At the end of the year, the intake and powerhouse structures were substantially completed.

As we now have the powerhouse building constructed and enclosed, we will continue the work on the assembly and

installation of the four generating units inside the powerhouse. Last year we reached an important milestone: we completed the South and North Spur dams, two of the three dams required to create the Muskrat Falls reservoir. We also made significant progress on the North dam.

POWERHOUSE / TRAILRACE

137,215 m³ of concrete placed to build the 84 m tall and 78 m wide structure



POWERHOUSE / INTAKE

144,696 m³ of concrete placed to build the 56 m tall and 143 m wide structure



NORTH DAM

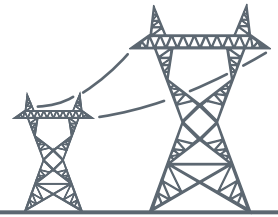
40% of the required concrete placed - reaching an elevation of 15.69 m



The transmission project remains on target to bring power from Labrador to the island in mid-2018.

We also achieved significant progress on the transmission project. We completed construction on the Labrador-Island Transmission Link (LIL) travelling 1,100 kilometres from Muskrat Falls in Labrador to Soldiers Pond on the Avalon Peninsula. This achievement marked the completion of all transmission line construction required for the project including the Labrador Transmission Assets and the Strait of Belle Isle Marine Cable Crossing.

TRANSMISSION



Project team members developed and executed major planning to ensure the safe delivery of the final key pieces of electrical equipment, including the massive transformers, rotors and stators, required at Muskrat Falls and Soldiers Pond, and which have been under construction for years. We achieved this and began the installation work as each piece was delivered. As construction continued on the switchyards and converter stations, work began on energizing the transmission assets.



SOLDIERS POND TRANSMISSION YARD

20 pieces of heavy equipment safely delivered to Soldiers Pond and Muskrat Falls



SOLDIERS POND - SWITCHYARD

Soldiers Pond AC switchyard completed and connected to the provincial electrical system



LABRADOR-ISLAND TRANSMISSION LINK - TRANSMISSION TOWER

3,224 towers assembled and erected using 45,000 metric tonnes of steel and 13 million bolts

Skilled Newfoundlanders and Labradorians Powering Our Province

Last year, more than 8,200 workers came together from over 480 communities across the province to apply their skills and expertise to help us reach 89 per cent construction completion on the Muskrat Falls Project. Thanks to their hard work and dedication, we reached numerous construction milestones this year.

A DIVERSE WORKFORCE DRIVING SUCCESS

We believe our province and society as a whole benefits from a diverse and inclusive work environment where different perspectives combine to push our entire team to its fullest potential.

We are proud that the total number of Newfoundlanders and Labradorians working on our project in 2017 included over 940 women and over 700 workers who identified as Indigenous.

In March 2017, we reached an important employment milestone and celebrated with our project partner, Innu Nation, the outstanding achievement of one million hours worked by Innu Nation members since the start of project construction.

BUILDING STRONG COMMUNITIES

It is not just our talented workforce which has contributed to the Muskrat Falls Project; local communities and businesses have also played a significant role over the years.

Early in the project, while working with governments and Labrador Indigenous groups, we recognized the need to build local capacity in Labrador where the majority of the project was being built. Seven years ago, the Labrador Aboriginal Training Partnership was established to support





education and training initiatives to help Labrador Indigenous people gain the skills and qualifications needed for employment opportunities with the project.

To date, more than 1,100 Indigenous people have found employment related to the project.

We are dedicated to building strong relationships with the people of the province, Indigenous leaders and the communities where we operate. We continuously work to develop partnerships that will provide long-term benefits for the people of our province.

This year, we worked with nearly 400 local businesses, communities and organizations in relation to the work activities of the project.

Their support has helped us build and strengthen our relationships with communities across the province. These partnerships have contributed significantly towards progressing the construction project to where it is today.

We continue to strive to provide safe and exciting work and business opportunities to the dedicated, hard-working Newfoundlanders and Labradorians who help make up our team on the Muskrat Falls Project as we move towards powering our province in 2018 and beyond.



(TOP LEFT) Valard crew prepares final piece of transmission wire for stringing on the Labrador-Island Transmission Link

(RIGHT) Some of the many skilled workers who are part of the Muskrat Falls Project construction team.

Newfoundland and Labrador Hydro

ENERGY YOU CAN COUNT ON



**STRENGTHENING
THE PROVINCE'S
ELECTRICITY SYSTEM,
NOW AND FOR
THE FUTURE**

Our Customers are
at the Heart of
Everything We Do

Approximately
9 out of 10



residential customers
surveyed are satisfied
with service

85%

satisfaction rate among
commercial customers



CARING ABOUT OUR CUSTOMERS

Every hour, every day, the people and businesses of this province count on us to provide a reliable and safe supply of electricity. The service we provide keeps communities – large and small – working all over Newfoundland and Labrador.

Behind the scenes, Hydro employees work diligently to make sure our customers can carry on with their daily activities. We take our work and our responsibility seriously, and we are proud of the role we play in the province’s growth and development. Most importantly, our customers are the driving force behind our focus on quality improvement.

NEW PROGRAM FOR CUSTOMERS WITH CRITICAL NEEDS

Hydro’s Critical Customer Notification Program was designed to provide extra attention and communication to customers who have a greater reliance on electrical service, including people who depend on life support equipment, and agencies and institutions such as hospitals, which provide essential services that depend on electricity. Whenever we plan a power outage, we make every effort to contact those customers and organizations, so that they are adequately informed and able to prepare in advance.

SYSTEM MAINTENANCE AND RELIABILITY

In 2017, more than **150** projects were completed and close to **5,000** activities were carried out on our equipment and facilities.

STRENGTHENING THE PROVINCE'S ELECTRICITY SYSTEM, NOW AND FOR THE FUTURE

As a regulated utility, we remain focused on our core responsibility to provide electricity to Newfoundlanders and Labradorians in a safe, reliable and cost-effective way.

As part of that mandate, we are committed to delivering on our promise to our customers today, while managing the evolving needs of tomorrow with an integrated, interconnected electrical system.

INVESTING IN ELECTRICITY ASSETS AND DELIVERING RELIABLE SERVICE

Ensuring that we are in a position to serve our customers reliably means we must invest responsibly to maintain our electricity assets throughout the province. We focus on balancing our customers' need for reliability with our responsibility to be strategic and cost-effective in planning and decision-making.

In 2017, we built critical new transmission infrastructure to increase system resiliency and improve reliability. This included a substantial upgrade to the Bay d'Espoir-to-Avalon Peninsula transmission corridor with the completion of a new high voltage line, as well as ongoing construction of a transmission line from the Hardwoods terminal station to Soldiers Pond.

Our transmission and operations teams were instrumental in integrating new transmission assets and equipment for

the Bottom Brook terminal station in western Newfoundland and at Soldiers Pond on the Avalon Peninsula. This work also adds to the stability and reliability of the island interconnected electricity system.

We refurbished a number of terminal stations in 2017. This included upgrades to power transformers in Cat Arm, Western Avalon, Hardwoods, Holyrood and Paradise River. Breaker replacements and refurbishments were completed in several locations, including Holyrood, Churchill Falls, Buchans, Bear Cove and Plum Point. Maintenance and upgrades were also carried out on various distribution systems and remote diesel plants in the province's most isolated service areas.

An overhaul of the 27 MW gas turbine serving Happy Valley-Goose Bay and region was completed last year. We

also continued to make necessary investments to upgrade and refurbish the Bay d'Espoir and Holyrood generating stations to ensure the reliable operation of these key facilities.

MODERNIZING THE PROVINCE'S ELECTRICITY NETWORK

As our electricity grid evolves and becomes interconnected to the rest of North America, the demands on our system continue to grow.

The Newfoundland and Labrador System Operator (NLSO) advanced its role of overseeing and managing the safe, reliable operation of the province's bulk electricity system, 24 hours a day. The NLSO does this by monitoring consumption load, overseeing system risks and requirements, and striking a balance constantly between supply and demand.

MARCH WINDSTORM

In early March 2017, a winter storm unleashed hurricane-force winds on many parts of Newfoundland and left tens of millions of dollars' worth of damage in its wake. Hydro's electrical infrastructure and our employees were tested during and after the storm. Our dedicated crews worked around the clock in extreme weather conditions to repair damage and restore power to customers as quickly and safely as possible, and to secure the electricity system after the storm subsided.



CELEBRATING HISTORIC ACHIEVEMENTS IN OUR PROVINCE'S ELECTRICITY SYSTEM

BAY D'ESPOIR: POWERING OUR PROVINCE SINCE 1967

The Bay d'Espoir hydroelectric generating facility marked its golden anniversary in May, recognizing 50 years since power first flowed from the plant in 1967.

The Bay d'Espoir facility is an integral part of our electricity system and our province's history. Before the plant was built, almost 75 per cent of homes in rural communities in Newfoundland were still without electricity. Construction of the facility marked the momentous first step towards electrification of the province.

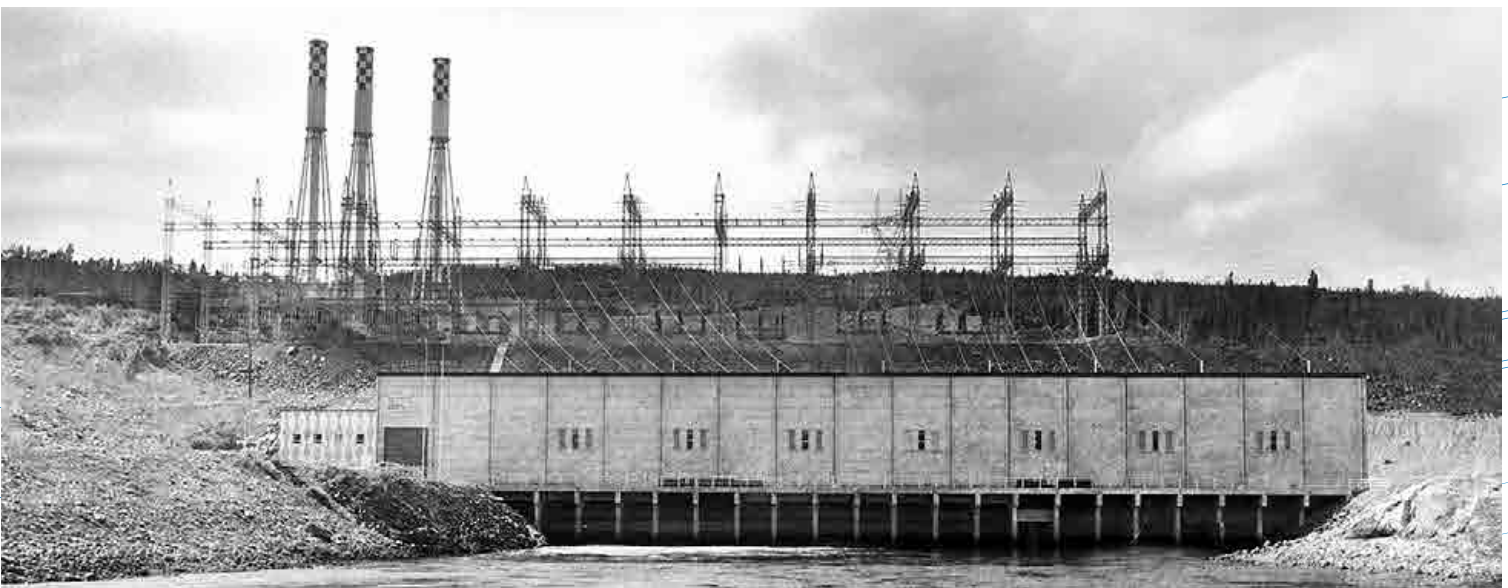
Bay d'Espoir continues to be a critical component of our electricity network today, providing clean, renewable energy to customers in communities throughout Newfoundland.

Aside from the plant itself, 832 kilometres of high-voltage transmission lines were also built, connecting St. John's, Bay d'Espoir, Grand Falls, Corner Brook and Stephenville. This formed the backbone of our provincial electricity grid, allowing distribution of power and playing a key role in rural electrification efforts. Today, Hydro has over 3,700 kilometres of transmission lines across the island.



(RIGHT) On August 3, 1965, the Honourable Joseph R. Smallwood and some local children from St. Alban's officially turned the sod to start construction of the Bay d'Espoir Hydroelectric Development.

(BELOW) When the plant was commissioned in 1967, four units were brought online. With continued growth in the province, an additional three units were added and today the plant provides over 600 MW of power.



BUILDING NEW TRANSMISSION CAPACITY FROM BAY D'ESPOIR TO THE AVALON PENINSULA

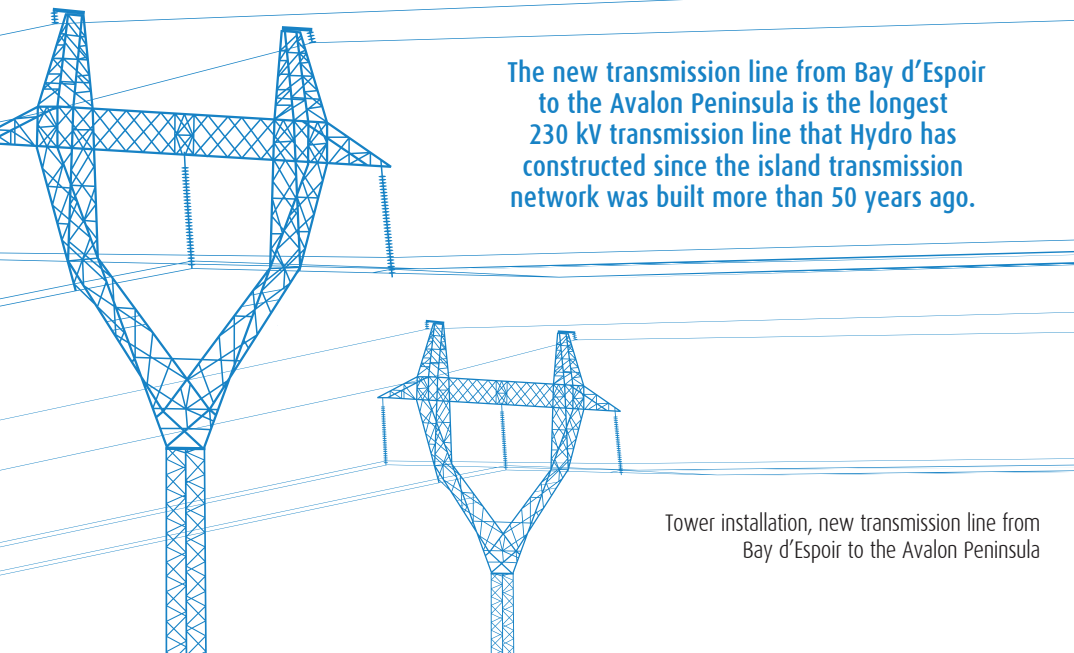
In late 2017, Hydro expanded the provincial electricity network with the completion of the third major 230 kV transmission line from Bay d'Espoir to the Avalon Peninsula. This line runs along the same corridor as the

original transmission lines built during construction of the Bay d'Espoir facility. Construction began in the summer of 2016, and the project was completed on schedule.

With this new transmission asset, we have greatly increased capacity into the Avalon – making the province's electricity system, and our ability to serve our customers, stronger and more reliable.



Hot line crew during transmission line construction in 1966.



The new transmission line from Bay d'Espoir to the Avalon Peninsula is the longest 230 kV transmission line that Hydro has constructed since the island transmission network was built more than 50 years ago.

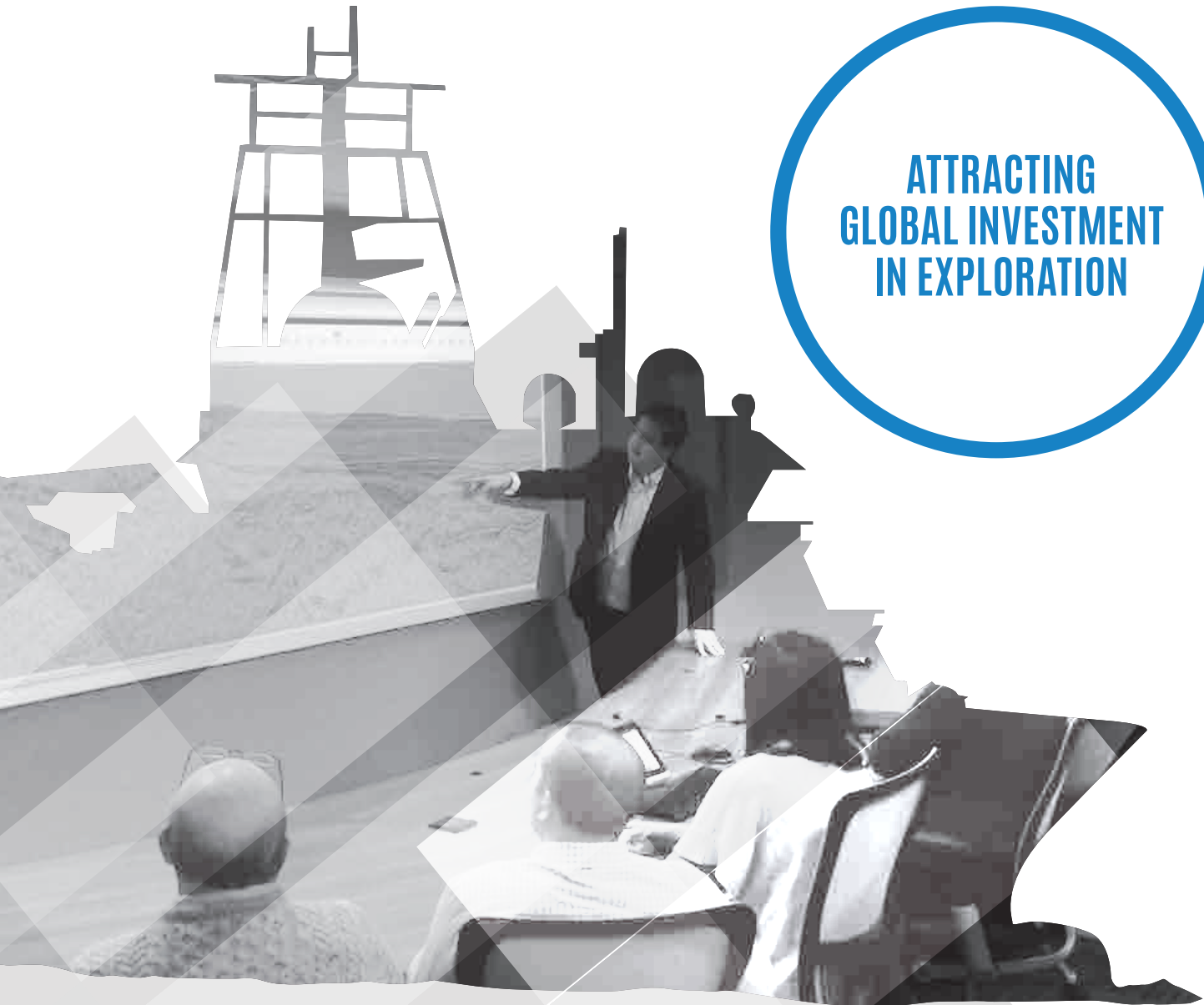
Tower installation, new transmission line from Bay d'Espoir to the Avalon Peninsula



Oil and Gas

PROVEN RESOURCES WITH TREMENDOUS POTENTIAL TO GROW

**ATTRACTING
GLOBAL INVESTMENT
IN EXPLORATION**



We're working every day to ensure the responsible development of our energy resources, long-term employment opportunities and a strong future for Newfoundland and Labrador.



**HEBRON PLATFORM
TOWED TO FIELD**

**CONSTRUCTION OF
WEST WHITE ROSE
STARTED**

**OVER 170,000
LINE KILOMETRES
OF 2D DATA COLLECTED
- SINCE 2011**

**\$2.55 BILLION
IN OPERATOR WORK
COMMITMENTS OVER LAST
THREE YEARS AND SEVEN
NEW ENTRANTS**

Building on the strength of our people and the potential of our natural resources, momentum in Offshore Newfoundland and Labrador (Offshore NL) continues to grow. As multinational companies look for opportunities to meet global demand for oil, our offshore frontier basins offer tremendous potential. We've only just begun to realize the full potential of our offshore to maximize the benefit of our natural resources for the people of our province.

We have a unique combination of experience and proven resources, coupled with untapped potential. Our people include a highly skilled and dedicated workforce with decades of experience, supporting four producing oil projects. Our province has the existing infrastructure necessary to support oil and gas fabrication, and globally, we are an attractive place

to do business, thanks to our access to deep waters, stable policies and an established supply chain.

PRODUCING PROSPERITY FOR OUR PROVINCE

Completion of the Hebron Platform
After five years of construction, and an impressive 40 million hours of worktime with no lost time injury, thousands of hard working Newfoundlanders and Labradorians contributed to the completion of the Hebron platform. The Hebron Platform was towed to field in June and produced first oil on November 27.

It is estimated the field will produce more than 700 million barrels of recoverable resources, and with a 4.9 per cent equity stake, this will contribute revenues to the province.



PRODUCTION

4 major producing projects, planned expansions ongoing.



EXPLORATION

650 new leads and prospects with over 20 basins.

Newfoundland and Labrador is on the verge of a new era in frontier oil exploration and development. Buoyed by recent discoveries, proven production and robust industrial and supply servicing capabilities, the province's resources are attracting the attention of the global industry.

WEST WHITE ROSE PROJECT ANNOUNCED IN MAY

Creating new job opportunities, the West White Rose project started construction in late 2017, with first oil expected in 2022. Nalcor holds a 5 per cent equity stake in the development along with partners Suncor Energy and lead operator Husky Energy.

The project is anticipated to achieve a gross peak production rate of approximately 75,000 barrels per day in 2025.

EXPLORING OUR FULL POTENTIAL

Frontier Exploration

Our oil and gas resources are among the richest in the world and we work every day to manage these resources for the maximum benefit of the people of the province. Even after 30 years of producing oil and gas, Offshore NL remains largely unexplored and our exploration team is focused on evaluating and de-risking these offshore oil and gas opportunities.

Partnering with World Class Experts

Working with experienced seismic partners TGS and Petroleum

Geo-Services, we collected 9,100 square kilometres of 3D seismic data and 20,000 line kilometres of 2D in 2017, for a total of over 170,000 line kilometres of 2D seismic data collected to date. We also partnered with Fugro to acquire approximately 10,000 square kilometres of multibeam bathymetry and over 100 seabed cores in the upcoming license rounds areas. This information will be shared with the global industry in advance of the Call for Bids scheduled for November 2018, bringing us closer to unlocking the potential of our province's oil and gas resources.

CAPTURING OFFSHORE INSIGHTS

Our Nalcor Exploration Strategy System (NESS) is a web-based application, the first of its kind in Newfoundland and Labrador, that provides a wealth of information from multiple sources, studies and reports within an interactive map. Users are able to display, filter and analyze a vast array of data and information in one location. Last year, we launched an updated version of NESS. This information is available to global and local industries, academic institutions and the public to inform their understanding of Offshore NL.

CREATING THE FOUNDATION FOR OUR PROSPEROUS ENERGY FUTURE

Offshore oil and gas projects in Newfoundland and Labrador are a key part of the foundation for our province's prosperous energy future. We're working every day to ensure the responsible development of our energy resources, long-term employment opportunities and a strong future for Newfoundland and Labrador.

To date, our efforts have resulted in over 650 leads and prospects and new basin areas, and despite an economic downturn, we have helped create \$2.55 billion in exploration work commitments over the last three years, including investment by seven new exploration and production companies.

By leading exploration activity in the early stages of the exploration cycle and providing extensive information about our offshore resources, we are opening new areas for industry exploration and potential future development of our oil and gas resources.

Unlocking Newfoundland and Labrador's Oil and Gas Potential

Our exploration team is focused on finding and quantifying new oil and gas potential for the people of Newfoundland and Labrador.

With a commitment to unlocking the potential of Newfoundland and Labrador's vast oil and gas resources, Nalcor Energy's exploration team was honoured to be shortlisted for Exploration Company of the Year by the Petroleum Economist in November 2017.

This global award celebrates the people, companies and projects which epitomize the best of the energy industry. Specifically, the Exploration Company of the Year award recognizes a company that has demonstrated an enterprising attitude and pursued its business interests successfully, using innovative techniques or processes.

Until recently, little was known about many of the frontier basins offshore Newfoundland and Labrador. Our exploration team has been guiding a strategy founded in the collection of state-of-the-art geoscience data with



the goal of finding and quantifying new oil and gas resource potential for the people of our province.

Since launching our exploration strategy, we've continued to attract new investment. Seven new international companies have entered our offshore in the last two years.

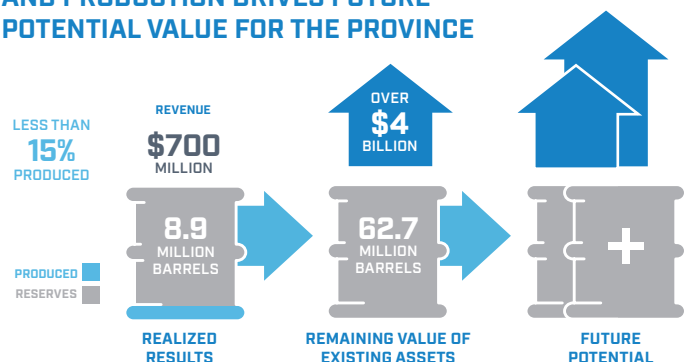
POTENTIAL GROWTH

Since first oil in 2010, Nalcor Energy has produced less than 15 per cent of its total reserves, yielding over \$700 million in revenue. Nalcor's equity re-investment into seismic further grows the future potential of our province's oil and gas resources.

Buoyed by recent discoveries and a proven track record of production, our province's resources are attracting global attention and we have the skilled workforce and robust industrial capabilities to deliver.

We are just starting to understand the full potential of our resources and we're excited to work together with industry, government, academia and local communities to maximize the benefit of our natural resources for the people of our province.

EQUITY RE-INVESTMENT IN EXPLORATION AND PRODUCTION DRIVES FUTURE POTENTIAL VALUE FOR THE PROVINCE



OUR BUSINESS

Offshore Newfoundland and Labrador is Rich in Oil and Gas Resources

Newfoundland and Labrador's oil and gas resources are among the richest in the world. We work every day to manage these resources for the maximum benefit of the people of our province.

There is tremendous potential in Newfoundland and Labrador's offshore. To put it in context from a geographical perspective – our offshore area is one and a half times the size of the Gulf of Mexico.

So far, our independent resource assessments have identified an in-place potential of 37.5 billion barrels

of oil and 133.6 trillion cubic feet of gas in just two areas that make up less than five per cent of the province's offshore area.

Compared to other oil and gas jurisdictions like the UK and Norway, our offshore resources remain largely unexplored. Less than seven per cent of our 1.8 million square kilometres of offshore area has been licensed, creating frontier opportunities for exploration and future development.

To help unlock our next potential development, Nalcor's exploration team is executing an exploration

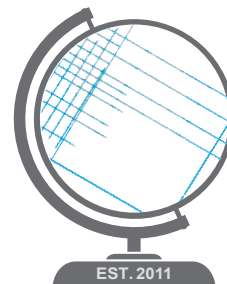
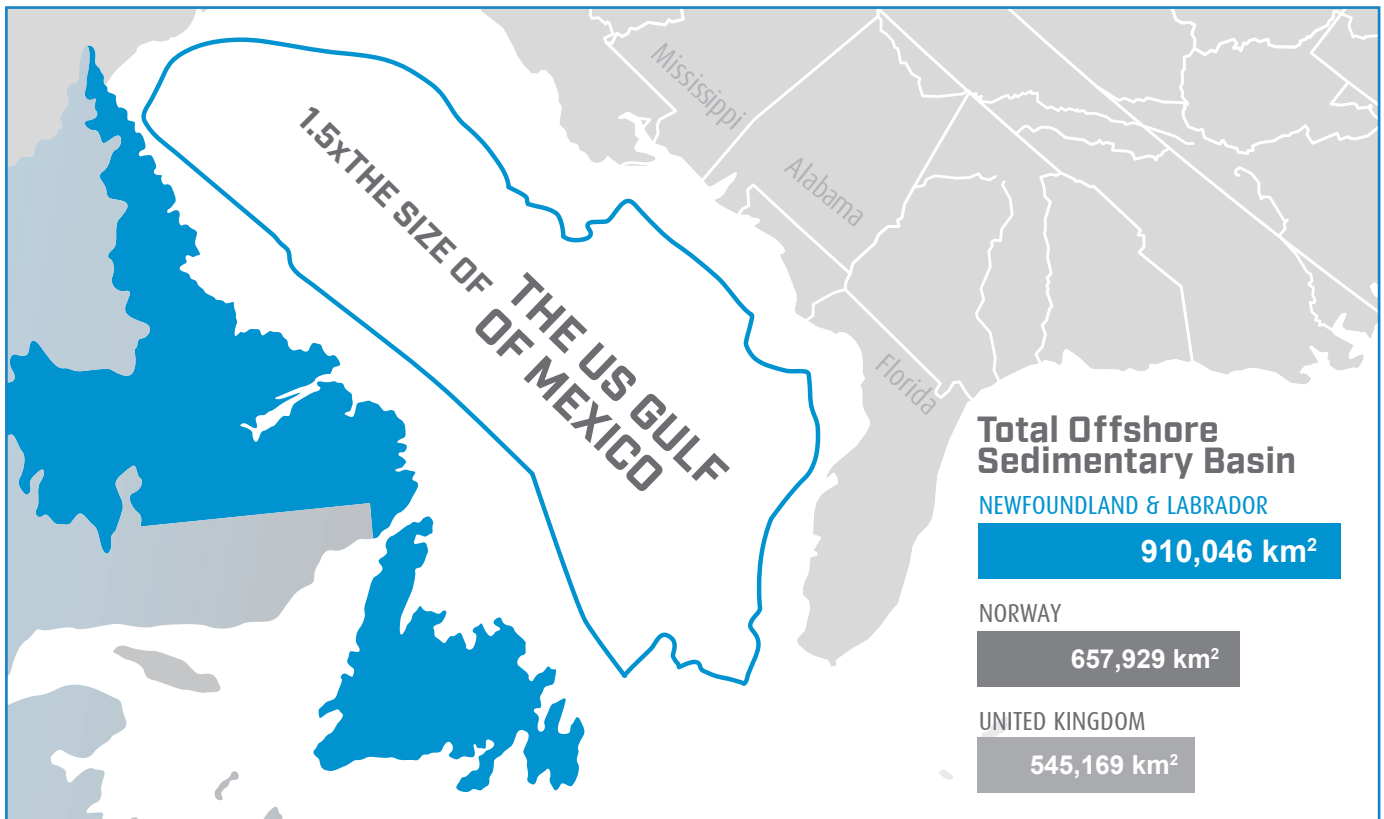
program which to date includes the collection of more than 170,000 line kilometres of 2D seismic data and over 15,000 square kilometres of 3D seismic data throughout the offshore.

Our exploration program has led to the identification of more than 650 leads and prospects. The Cape Freels prospect was identified in 2016 in the West Orphan Basin and is one of the largest undrilled prospects in the world.

In addition to our vast potential, our skilled workforce and strategic location makes Newfoundland and Labrador a globally competitive and preferred location for oil and gas investment.

OUR PLACE

OUR OFFSHORE IS ONE AND A HALF TIMES THE SIZE OF THE GULF OF MEXICO



EST. 2011

OUR ONGOING
SEISMIC
PROGRAM IS
ONE OF THE
LARGEST
IN THE WORLD

OVER **170,000** LINE KM

OF NEW 2D MULTI-CLIENT DATA
ACQUIRED BY THE END OF 2017

Bull Arm

WORLD CLASS FABRICATION CAPABILITIES



The site spans
OVER 6,300 ACRES
supporting simultaneous
fabrication and assembly
in three key areas:



FABRICATION
YARD



MARINE
FACILITY



DEEPWATER
SITE

Bull Arm is Atlantic Canada's largest fabrication site with world-class assets and a history of supporting the development of Newfoundland and Labrador's oil and gas sector.



A KEY SITE FOR OUR OIL AND GAS INDUSTRY

Originally built to fabricate the Hibernia Offshore Oil Project, the Bull Arm Fabrication Site was constructed in the 1990s. Since then, thousands of hard working Newfoundlanders and Labradorians have played a significant role in the construction of four offshore projects at the Site, most recently the Hebron Project.

Construction of the multi-billion dollar Hebron Project began at the Site in 2011 and included the construction of 130,000 cubic metre concrete Gravity Based Structure (GBS) platform, fabrication of the living quarters and integration of its topside modules. In 2017, the Hebron Project reached construction completion at Bull Arm and was towed to field in June resulting in Nalcor's lease with ExxonMobil Canada Properties concluding on December 31, 2017.

GROWTH OF OUR INDUSTRIAL SECTOR

In preparation for the conclusion of the lease, the Bull Arm team began to assess what may be next for the Site. Throughout 2017, meetings were held with local, national and international stakeholders and marketing materials were developed and distributed that highlighted the Site's capabilities.

In March, a request for Expressions of Interest (EOI) was issued across local, national and international markets to invite and evaluate potential future opportunities for the Site. A number of EOI submissions were received and included proposals for activities associated with such things as industrial fabrication, supply servicing and marine operations.



(TOP) Tow-out of the Hebron platform from the Bull Arm Construction Site - June 3, 2017

Chain cutting ceremony on the Hebron platform with ExxonMobil and the project co-ventures

The information collected through the EOI helped inform the release of a formal Request for Proposals (RFP) in October. The Bull Arm team remains focused on securing a tenant, or multiple tenants, who will maximize the benefit of this asset for the people of our province and attract sustainable business opportunities to allow the Site to continue to play a part in the growth of our industrial sector.

Coming Together for Our Communities: Bull Arm Holiday Donation

Being an engaged, valued corporate citizen is a priority for Nalcor. We live this value by supporting organizations in the communities in which we work and where our employees live. We also encourage and support our employees to give back to their communities in Newfoundland and Labrador.

Our employees are the core of our community investment program. They dedicate time and effort to volunteer, raise funds and donate items of need to organizations across the province.

Last year, when the Hebron Project finished at the Bull Arm Fabrication Site, we gained ownership of the living quarters as a result of the close-out of the lease agreement with ExxonMobil. This meant we also acquired a number of kitchen, household and office items.

Our Bull Arm team immediately saw the opportunity to reach out to not-for-profit organizations across the province providing food and shelter services, which could make good use of the items available.

We contacted those not-for-profit organizations to identify their interest in the items available. We received many applications from across the province. We supported 23 organizations representing a variety of groups and they were delighted to be included in this donation.



The donation will help us serve more than 16,000 meals, and support the furnishing of thousands of requests for housing assistance each year.

Jessica Rockwood
Administration and Gift Management Officer
Choices for Youth



(L-R) Members of the Bull Arm team at The Gathering Place for donation launch

Delivering one of the 500 mattresses with Home Again Furniture Bank

*Coming Together
for Our Communities*
and 23 organizations across the province:

PROVINCIAL

AIDS Committee NL	John Howard Society
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ST. JOHN'S & SURROUNDING COMMUNITIES

Choices for Youth	Jimmy Pratt
Home Again Furniture Bank	Memorial Outreach Centre
The Gathering Place	Stella's Circle
Iris Kirby House & O'Shaughnessy House	St. John's Native Friendship Centre

CENTRAL

Cara Transition House	Salvation Army Gander
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LABRADOR

Libra House	
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BULL ARM & SURROUNDING COMMUNITY GROUPS

11 Community Groups

Over a thousand people in St. John's live on the streets or in hostel boarding houses and we are expecting these numbers to continue to increase. Nalcor Energy's generous donation of large scale appliances and other kitchen items will help The Gathering Place meet this growing need.

Joanne Thompson,
Executive Director
The Gathering Place

Energy Marketing

SELLING NEWFOUNDLAND AND LABRADOR'S SURPLUS ELECTRICITY



99%

**OF AVAILABLE
RECAPTURE ENERGY
DELIVERED TO MARKET**

We continue to pursue opportunities to optimize the value of the province's surplus electricity by actively participating in energy markets in eastern Canada and the United States.

SOLD ENERGY
to New York,
New England, Ontario
and the Maritimes



NEW CONTRACTS
to purchase energy
from outside
Newfoundland and
Labrador to achieve
COST SAVINGS



Last year, 99 per cent of available recapture energy was delivered to market. Approximately 1.6 terawatt hours of recapture energy from Churchill Falls was sold to customers in New York, New England, Ontario and the Maritimes realizing revenues of \$47 million.

CONNECTED TO THE NORTH AMERICAN GRID

The domestic electricity market in Newfoundland and Labrador realized a historic first in December 2017 when the inaugural flow of energy across the Maritime Link marked the connection of the island of Newfoundland to the North American grid. The planned completion of the Labrador-Island Transmission Link (LIL) in mid-2018 will also connect the island portion of the province to Labrador.

In advance of the completion of these new transmission assets, we completed readiness activities to allow us to optimize the value of

our electricity assets and further participate in energy trading activities outside of Newfoundland and Labrador.

MAXIMIZING BENEFITS FOR THE PEOPLE OF NEWFOUNDLAND AND LABRADOR

In early 2018, we entered into a short-term agreement with our affiliate Newfoundland and Labrador Hydro to facilitate energy imports from outside of the province to displace fuel at the Holyrood Thermal Generating Station.

We also have agreements with various market participants that enable energy purchases when there are cost savings to be realized. We will continue to assess all opportunities to acquire lower-cost electricity in close coordination with Newfoundland and Labrador Hydro to determine the best option for Newfoundland and Labrador's electricity customers.

Churchill Falls

ONE OF THE LARGEST HYDROELECTRIC GENERATING FACILITIES IN THE WORLD



8 CONSECUTIVE YEARS

100%

Environmental Management System
TARGETS COMPLETED

On average, the facility generates over 31 terawatt hours of energy annually – roughly one per cent of the world’s hydroelectric power



99%

Execution of key and critical maintenance programs

96.9%

Guaranteed Winter Availability Contract (GWAC) met

10x 

Ten of the original transformers replaced

Marking the completion of our multiyear Generator Step Up (GSU) Replacement Program.

Maintaining the massive Churchill Falls hydroelectric facility through yearly capital projects and operating programs requires careful and strategic coordination of diverse teams whose focus is dedicated to safe and successful execution of critical projects necessary to maintain this world-class facility.

There is a great deal of work to plan, schedule and execute within a maintenance season consisting of a mere seven months. On average, nearly 100 distinctive projects and programs are planned each year to ensure this flagship operation continues to operate safely and

successfully today, tomorrow, and for many years to come.

In 2017, 95 per cent of the 82 planned projects at Churchill Falls were safely and successfully completed under budget, meeting their completion target.

Over the last decade, we began placing stronger emphasis on improving the execution and completion rates of both the capital and operating projects and programs for Churchill Falls. Since that time, its completion performance rates have increased by nearly 60 per cent and these continue to improve with each passing year.



95% of planned capital and maintenance projects safely and successfully completed under budget.

Churchill Falls Generating Station is not your typical hydroelectric station

Churchill Falls Generating Station is the second largest underground hydroelectric plant in North America and one of the largest underground powerhouses in the world.

It's not your typical elevator ride down to the ground floor — it's nearly a full two-minute ride that carries you 1,000 feet under the ground.

As the elevator doors open, it's the faint humming of electricity production that you notice as you step out into a hallway of solid

three billion year-old granite. Beyond the door, just a short walk down the granite hallway, is one of the greatest engineering marvels of its time — the Churchill Falls underground hydroelectric station.

The sound grows louder through your ear protection as the metal door opens. You gaze down the concrete hallway surrounded by the walls of continuous solid granite — excavated by thousands of workers beginning in 1967.

Eleven massive transformers sit in a row stretching about 850 feet down the concrete hallway. They are increasing voltage from the generating units that produce clean, renewable energy which travels thousands of kilometers to millions of customers across North America each day.

Beyond the six million pound generators and through massive granite tunnels you will find the rest of this magnificent powerhouse measuring 15 stories high and nearly 1,000 feet long, or slightly longer than three Canadian football fields.

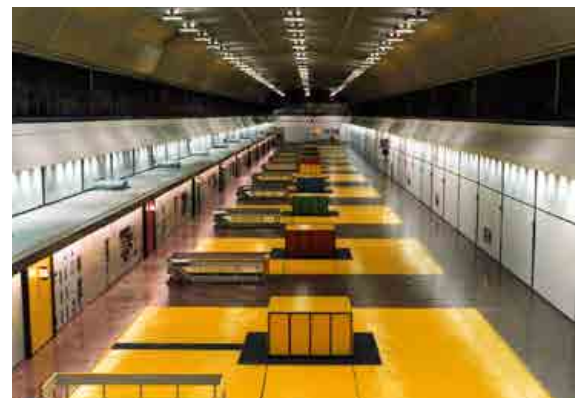
**OUR
BUSINESS**



Within these tunnels and wide-open spaces are the generator floor, surge chamber, water storage gallery, two tailraces and a number of control and work stations necessary to maintain this flagship operation.

Beneath the vibrantly coloured covers on the generator floor are eleven turbines spinning at 200 revolutions per minute generating 5,428 MW of energy. These generators connect to the 11 transformers behind a wall of control panels which are monitored daily by the plant's skilled and dedicated employees.

As you travel back to the surface, the not-so-typical elevator ride doesn't seem so long. The elevator doors open and you step into the office building, knowing you have truly felt the magnificent power of our energy system sitting just 1,000 feet below your feet.



(L-R) In 1967, thousands of workers began the excavation of the underground powerhouse, the heart of the Churchill Falls Generating Station.

Eleven massive transformers sit along this hallway of three billion year-old granite.

The generator floor is where 11 turbines, spinning at 200 revolutions per minute, harness the power of the massive Churchill River, with a generating capacity of 5,428 MW.



Community

COMMITTED TO OUR COMMUNITIES

Supporting communities where we work and where our employees live

Through our Community Investment Program, we provide philanthropic support to address the needs of the communities in which we work and where our employees live.

Annually we provide approximately \$640,000 in charitable funding to more than 20 not-for-profit organizations across Newfoundland and Labrador.

We support communities by funding programs that support our three investment priorities: youth leadership and anti-bullying; child and youth education initiatives; and youth safety and diversity and inclusion initiatives.

YOUTH LEADERSHIP AND ANTI-BULLYING



>\$250,000

CHILD AND YOUTH HEALTH SAFETY AND DIVERSITY AND INCLUSION



>\$200,000

CHILD AND YOUTH EDUCATION



>\$40,000



EVERY YEAR our employees give generously of their time, skills and talents to support important causes in our province by helping those who need it most. Volunteerism is an integral part of our commitment to the communities where we live and serve. Our employees and retirees volunteer countless hours throughout the entire province.

COMING TOGETHER FOR OUR COMMUNITIES



In partnership with the Canadian Red Cross, we distributed more than 10,000 shirts to more than 40 schools across Newfoundland and Labrador for Pink Shirt Day.



Our employees volunteered 3 hours per week for 12 weeks at the Jimmy Pratt Outreach Centre and Soup Kitchen, preparing and serving hot meals to their patrons.



We adopted two rooms at Ronald McDonald House through the Adopt-A-Room Program which allows the House to provide upkeep to the rooms over the next three years.



As a visionary child and youth partner with the Heart & Stroke Foundation, Hydro continued to play a pivotal role in educating youth in the province about healthy eating.



Our Bull Arm team volunteered countless hours and donated kitchen, housing and office items to over 23 organizations across Newfoundland and Labrador.



During Acts of Kindness Week our employees volunteered their time supporting over 20 community groups:

- Delivering meals to 55 people through Meals on Wheels
- Serving a healthy breakfast to close to 1,000 students through Kids Eat Smart
- Collecting and donating enough furniture for ten homes through Home Again Furniture Bank
- Sorting food and clothing for the Community Food Sharing Association and the Single Parents Association of Newfoundland

There's No Place Like Home

There's something special about how you feel when you walk through the doors of Ronald McDonald House Newfoundland and Labrador (RMHNL). You can't quite put your finger on it until you've spent some time there. It begins with the friendly smile you get from the volunteers and employees at RMHNL and it grows with the time you spend with the children and families who are staying at the House.

Nalcor Energy and Hydro have been active supporters of Ronald McDonald House from the day it opened. We started with the capital campaign; later, we took on the role of presenting sponsor of the Red Shoe Crew Walk for Families (NL Hydro). Since then, our people have been there every step of the way including McHappy Day, Adopt-A-Room Program, Just like Nan's, Home for Dinner, and the Sock-it Campaign.

In the House, there are family rooms, or suites where families can stay for as long as they need. It's a place they find support, a place where they can be together as a family, a true home away from home. Nalcor and Hydro have adopted two suites through the

Adopt-A-Room program. This program allows organizations to pay for the upkeep and maintenance of a family suite for three years.

A CLOSE CONNECTION

We met the family staying in the Hydro suite and learned something very special about this particular family; this family was one of our own. The son, daughter-in-law and two granddaughters of a long-term Hydro employee were away from home seeking medical treatment for their daughter. Unveiling the new name on the room - Hydro - was incredibly moving given the connection between this family and our company.

It was a beautiful room, cozy and comforting, with a teddy bear lying on one of the beds. It's hard to imagine what these families go through having a sick child, but knowing our Community Investment Program continues to support the health and safety of children in this province makes us proud.

There truly is something special about the way you feel when you walk through the doors of the Ronald McDonald House. Once you leave, you'll know what that feeling is - it's the feeling of being home.



People
DIVERSITY MATTERS

Our strength comes from our dedicated team of employees who are committed to serving the people of Newfoundland and Labrador.

BUILDING A DIVERSE AND INCLUSIVE WORKPLACE

We are committed to a work environment where our employees feel valued, respected, engaged and empowered to reach their full potential. We have diversity and inclusion, employee engagement and talent management frameworks in place to support this commitment. Throughout 2017, we developed and implemented strategies to improve employee engagement company-wide. We also have a talent management framework in place with a focus on strategies to attract talent, support retention and develop our people.

We recognize how important it is to have a workforce that reflects the people and communities we serve. Diversity in perspective and experience supports innovation and excellence in our work.



OUR EMPLOYEES CHAMPION DIVERSITY AND INCLUSION

As part of our commitment to diversity and inclusion, we created an internal Diversity and Inclusion Champions committee (above) in September 2017. The committee includes employees representing various levels, occupations and geographic locations across the company. Their role is to increase awareness about the value of diversity and inclusion and how they contribute to building a diverse and inclusive workplace culture.

GENDER EQUITY

In 2017, we set gender equity targets to increase the representation of women in occupations in which they are under-represented. To support these targets, along with our broader commitment to encourage opportunities for women, Indigenous peoples, persons with disabilities, and members of visible minorities, we undertook a review of our recruitment

and talent management processes. Our proactive efforts to attract a diverse pool of qualified candidates also included actively engaging them in the screening process. As a result, we have made progress in increasing female representation in several key areas, including management and skilled trade apprentices.

SUPPORTING CAREER DEVELOPMENT FOR WOMEN

In January 2017, we launched an internal Women’s Leadership Network (WLN). The role of the WLN is to facilitate professional development and networking opportunities focused on supporting career development and advancement for women. The WLN held sessions on a variety of leadership topics, panel events, webinars, and a roundtable discussion about women in operations. These activities raised awareness of the need for greater representation of women and promoted our commitment to diversity and gender equity.

WOMEN IN THE WORKFORCE

OCCUPATIONAL GROUP

	WOMEN		
	2016	2017	TARGETS
Executive	15%	15%	30%
Management	27%	32%	35%
Engineers (Including Engineers in Training)	24%	21%	30%
Technicians & Technologists	5%	6%	10%
Field Supervisors	3%	5%	6%
Skilled Trades (Including Apprentices)	2%	4%	10%
Manual Workers	16%	16%	20%

Environment and Sustainability

COMMITTED TO BEING A SUSTAINABLE PART OF THE COMMUNITY

We are fortunate to live and work in a province with an abundance of natural resources and pristine land.



We are committed to the safe and responsible management of our province's energy resources. Every day, our employees across the province come to work to help the company cultivate and sustain a diverse and healthy environment for Newfoundlanders and Labradorians.

To achieve our goals, all of our lines of business establish environmental targets. These targets support our focus on maintaining high levels of environmental compliance, responsibility and performance.

In 2017, we collectively set more than 100 targets and for the third consecutive year, we achieved 100% of our targets.

In 2017, we moved to the new ISO 14001 2015 standard for environmental management across the company, and we also successfully updated Nalcor's environmental management system to meet this new standard.

PROTECTING OUR PARKS AND NATURAL AREAS

We are fortunate to live and work in a province with an abundance of natural resources and pristine land. Recognizing we have a responsibility to mitigate our environmental footprint, Hydro updated its Environmental Protection Plan for work on transmission lines located within our parks and natural areas. We carried out considerable research to collect data from transmission lines and access trails to determine associated environmental sensitivities. Some of

these areas include stream crossings, bogs and wetlands; species at risk and species of concern; raptors; and areas of historic and cultural significance.

Through research and consultation with representatives from Parks Canada and the Government of Newfoundland and Labrador, we have developed and implemented procedures which take potential environmental impacts into account when planning our work. This is a powerful tool for our planners, supervisors and line crews and it forms the basis of a formal agreement with Parks Canada for Hydro work activities going forward. It also streamlines the process for Hydro crews who have work planned on any federal land in the region.

HIGHLIGHTS

COMMITTED TO MAKING IMPROVEMENTS

We always strive to learn and improve our response to potential environmental incidents. Following the 2016 spill at the Paradise River Hydro Generating Plant, Hydro implemented recommendations for improvements to our spill response. In 2017, Hydro completed the installation of a new General Electric Leakwise oil detection system at the plant in Paradise River. Based on this success, and following a review of potential spill sources, Hydro will install another system in 2018 in Bay d'Espoir. We continue to review other areas within the system for possible spill prevention opportunities.

In 2017, the Lower Churchill Project committed to improving Internal Awareness and Training within their Environment Regulatory Compliance team. The team developed, presented and provided learning opportunities in avifauna management training, spill response, sedimentation and erosion, and historic resources management. The awareness sessions allowed the team to discuss project monitoring and communicate with peers.

- Revised structure to reflect corporate reorganization for Nalcor and Hydro Environmental Management Systems.
- Formed a climate change mitigation and adaptation working group.
- Developed a framework and strategy for climate change.
- As part of a multi-year initiative, replaced 75 older and poor condition transformers in Hydro's Transmission and Rural Operations.
- Continued replacement of PCB-containing equipment in Churchill Falls, Transmission and Rural Operations, and Bay d'Espoir.
- Helped customers reduce electricity use by 2,631 MWh through Hydro's takeCHARGE programs.
- Engaged in idle reduction initiatives, including an employee awareness campaign.
- Completed more than 2,600 daily environmental monitoring reports and 11 detailed environmental audits across the Muskrat Falls Project in 2017.
- Completed new environmental targets database.

NALCOR RECEIVES CEA SUSTAINABLE ELECTRICITY AWARD

In November 2017, we received a Canadian Electricity Association (CEA) Sustainable Electricity Award for our work towards developing an integrated approach to sustainability.



OPERATING STATISTICS

Years ended December 31	2017	2016	2015	2014	2013
INSTALLED GENERATING CAPACITY (rated megawatts)					
Churchill Falls	5,428	5,428	5,428	5,428	5,428
Hydro - Hydraulic					
Hydraulic	956	956	956	956	939
Thermal	741	741	741	617	617
Diesel	67	66	66	64	53
Menihek	19	19	19	19	19
Total	7,211	7,210	7,210	7,084	7,056
ELECTRIC ENERGY GENERATED, NET (gigawatt hours GWh)					
Churchill Falls	30,927	33,806	33,470	32,192	34,536
Hydro					
Hydraulic	4,507	4,380	4,823	4,658	4,688
Thermal	1,725	1,740	1,500	1,316	956
Diesel	50	53	52	54	49
Menihek	45	46	46	48	45
Total	37,254	40,025	39,891	38,268	40,274
ELECTRIC ENERGY SALES (GWh)					
Churchill Falls Export	28,970	27,995	28,692	27,568	29,787
Hydro					
Utility	5,895	5,845	6,072	5,852	5,606
Rural	1,148	1,099	1,092	1,089	1,017
Industrial	2,386*	2,300*	2,231*	535	559
Export	1,578	1,649	1,645	1,545	1,514
Menihek Export	45	45	45	45	44
Twin Falls Industrial	-	-	-	1,607	1,683
Total	40,022	38,933	39,777	38,241	40,210
TRANSMISSION LINES (kilometres)					
Churchill Falls					
735 kV	608	608	608	608	608
230 kV	-	471	471	471	471
Hydro					
230 kV	2,267	1,609	1,609	1,609	1,609
138 kV	1,500	1,500	1,500	1,500	1,500
69 kV	634	634	634	634	634
Menihek					
69 kV	39	39	39	39	39
Total	5,048	4,861	4,861	4,861	4,861
PEAK ELECTRICITY DEMAND (megawatts)					
Churchill Falls	5,611	5,670	5,610	5,620	5,658
Hydro System	1,540	1,521	1,550	1,535	1,501
Island System	1,714	1,673	1,705	1,687	1,640
PETROLEUM AND NATURAL GAS PROPERTIES					
Oil Production (Thousands Barrels of Oil Equivalent (BOE)/day)					
White Rose Growth Lands	1.38	0.86	0.98	1.52	1.59
Hibernia Southern Extension	7.38	5.22	0.46	0.29	0.21
Hebron	1.10	-	-	-	-
Remaining Reserves (Proven and Probable) (Millions BOE)					
White Rose Growth Lands	8.43	5.66	2.85	3.63	4.50
Hibernia Southern Extension	18.20	23.53	24.98	25.10	21.35
Hebron	36.03	34.35	33.17	33.17	33.17
STAFFING LEVELS					
Full-time equivalents	1,528	1,490	1,460	1,394	1,334

*Includes sales former Twinco Bloc.

FINANCIAL STATISTICS

Years ended December 31 (millions of dollars)	2017	2016	2015	2014	2013
OPERATING RESULTS					
Revenue					
Energy sales	858	779	761	756	755
Other	72	45	50	42	30
	930	824	811	798	785
Expenses					
Fuels and power purchased	288	229	254	336	254
Operating costs ¹	219	207	244	249	212
Oil production, marketing and transportation costs ¹	36	26	12	-	-
Transmission rental and market fees ¹	25	22	22	-	-
Depreciation, depletion, amortization and impairment	300	135	159	93	90
Exploration and evaluation	1	2	1	1	7
Net finance expense	66	72	74	67	74
Other expense (income)	23	(4)	3	3	4
Share of loss (profit) in joint arrangement	-	-	-	(1)	(1)
Regulatory adjustments	(91)	(1)	58	(66)	57
	867	688	827	682	697
Profit (loss) for the year	63	136	(16)	116	88
Contributions to net income ²					
Hydro	36	16	(27)	19	4
Hydro Regulated	36	19	(26)	18	1
Hydro Non-Regulated	-	(3)	(1)	1	3
Power Development	(2)	(1)	(1)	(1)	(2)
Muskrat Falls	(2)	(1)	(1)	(1)	(2)
Power Supply	28	45	42	21	28
LCP Transmission	(1)	1	(2)	(1)	-
Churchill Falls	33	41	45	20	26
Other	(4)	3	(1)	2	2
Energy Markets	(37)	16	20	31	28
Energy Trading	15	17	21	32	29
Commercial and Other	(52)	(1)	(1)	(1)	(1)
Offshore Development	56	78	(32)	54	42
Oil and Gas	9	58	(49)	37	26
Bull Arm	47	20	17	17	16
Corporate and Other	(18)	(18)	(18)	(8)	(12)
FINANCIAL POSITION					
Total current assets	2,768	2,098	3,395	3,357	922
Total current liabilities	970	1,750	1,339	740	542
Net working capital	1,798	348	2,056	2,617	380
Property, plant and equipment, cost	15,749	12,414	9,202	6,307	4,305
Accumulated depreciation, depletion and impairment	1,195	997	877	648	562
Property, plant and equipment, net	14,554	11,417	8,325	5,659	3,743
Sinking funds (long-term portion)	229	230	282	267	238
Long-term investments	332	34	91	1,116	4,477
Regulatory deferrals (net)	38	(184)	(186)	(128)	(194)
Other assets	34	120	85	120	79
Long-term debt	9,386	5,873	6,008	6,241	6,048
Other liabilities	2,518	1,828	1,170	688	407
Shareholder's equity	5,081	4,264	3,475	2,722	2,268
CAPITAL EXPENDITURES³	3,424	3,286	2,790	2,035	1,037

¹Comparative figures have been reclassified to conform to the basis of presentation adopted during the current reporting period.

²The operating structure as at December 31, 2017 reflects organizational changes that resulted in revised operating segments effective January 1, 2017. The designation of segments is based on a combination of regulatory status and management accountability. Previously reported segmented information has been presented to conform with the current operating structure.

³Capital expenditures includes tangible and intangible expenditures.

EXECUTIVE, DIRECTORS AND OFFICERS

(listed as at Dec. 31, 2017)

NALCOR ENERGY EXECUTIVE

STAN MARSHALL
President and CEO

DERRICK STURGE
Executive Vice President, Finance and Chief Financial Officer

GILBERT BENNETT
Executive Vice President, Power Development

JOHN MACISAAC
Executive Vice President, Power Supply

JIM KEATING
Executive Vice President, Corporate Services and Offshore Development

NALCOR ENERGY BOARD OF DIRECTORS

BRENDAN PADDICK
Chairperson
CEO, Columbus Capital Corp.

JOHN GREEN²
Lawyer, McInnes Cooper

GEOFF GOODYEAR^{2, 4}
Retired

CHRISTOPHER HICKMAN^{1, 4}
CEO, Marco Group of Companies

JACK HILLYARD^{1, 3}
Retired BMO Executive

MARK MACLEOD^{2, 3}
President and CEO, C-Core

STAN MARSHALL
President and CEO, Nalcor Energy

BRIAN MAYNARD^{1, 3}
Retired Oil and Gas Executive

DEBBIE MOLLOY^{2, 4}
Vice President, Corporate Services, Eastern Health

DAVID OAKE^{1, 3}
President, Invenio Consulting Inc.

EDNA TURPIN⁴
Psychologist/Corporate Director

1/ Audit Committee 2/ Corporate Governance Committee 3/Human Resources and Compensation Committee 4/ Safety, Health, Environment and Community Committee

NALCOR ENERGY OFFICERS

STAN MARSHALL
President and CEO, Nalcor Energy

DERRICK STURGE
Executive Vice President, Finance and Chief Financial Officer

GILBERT BENNETT
Executive Vice President, Power Development

JOHN MACISAAC
Executive Vice President, Power Supply

JIM KEATING
Executive Vice President, Corporate Services and Offshore Development

PETER HICKMAN
Vice President, General Counsel and Corporate Secretary

CHRIS KIELEY
Vice President, Strategic Planning and Business Development

ROBERT HENDERSON
Vice President, Transition to Operations

MIKE ROBERTS
Chief Human Resources Officer and Vice President, Safety, Health and Sustainability

CARLA RUSSELL
General Manager, Finance

AUBURN WARREN
General Manager, Financial and Risk Management

MEREDITH BAKER
Assistant Corporate Secretary

EXECUTIVE, DIRECTORS AND OFFICERS

(listed as at Dec. 31, 2017)

NEWFOUNDLAND AND LABRADOR HYDRO LEADERSHIP TEAM

JIM HAYNES
President

LISA HUTCHENS
Vice President, Finance

DAWN DALLEY
Vice President, Regulatory Affairs and Corporate Services

TERRY GARDINER
Vice President, Engineering Services

RONALD LEBLANC
Vice President, Transmission, Distribution & NL System Operator

JENNIFER WILLIAMS
Vice President, Production

GEOFF YOUNG
Corporate Secretary and General Counsel

NEWFOUNDLAND AND LABRADOR HYDRO BOARD OF DIRECTORS

JOHN GREEN
Chairperson
Lawyer, McInnes Cooper

DONNA BREWER
Retired

HEATHER JACOBS
Retired

CHRIS LOOMIS
Professor (Retired), Memorial University of
Newfoundland and Labrador

STAN MARSHALL
President and CEO, Nalcor Energy

NEWFOUNDLAND AND LABRADOR HYDRO OFFICERS

STAN MARSHALL
President and CEO, Nalcor Energy

JIM HAYNES
President

LISA HUTCHENS
Vice President, Finance

DAWN DALLEY
Vice President, Regulatory Affairs and Corporate Services

TERRY GARDINER
Vice President, Engineering Services

JENNIFER WILLIAMS
Vice President, Production

GEOFF YOUNG
Corporate Secretary and General Counsel

SCOTT PELLEY
Corporate Treasurer

RONALD LEBLANC
Vice President, Transmission, Distribution & NL System Operator

MICHAEL LADHA
Assistant Corporate Secretary

CORPORATE GOVERNANCE

BOARD OF DIRECTORS

The principal functions of Nalcor Energy's Board of Directors include:

- (a) developing Nalcor's approach to corporate governance;
- (b) reviewing and approving the business, financial, strategic and other plans to enable Nalcor to execute its strategy;
- (c) adopting processes for monitoring the company's progress toward its strategic and operational goals;
- (d) approving the audited financial statements and Management's Discussion and Analysis;
- (e) ensuring that Management has a process for identifying the principal business risks;
- (f) overseeing the integrity of the internal control systems;
- (g) ensuring that Nalcor has processes for operating within applicable laws and regulations;
- (h) ensuring the company has a compensation philosophy and framework;
- (i) ensuring a process is in place to measure the performance of senior executives of Nalcor;
- (j) ensuring Management creates a culture of integrity throughout the organization; and
- (k) ensuring that succession plans are in place for senior Management, including the President and CEO.

The Board also has four committees:

1. Audit
2. Corporate Governance
3. Human Resources and Compensation
4. Safety, Health, Environment and Community

Nalcor has the following subsidiary companies (in addition to Newfoundland and Labrador Hydro), each with its own Board of Directors (listed as at Dec. 31, 2017).*

*Excludes currently inactive legal entities Gull Island Power Company Limited and Lower Churchill Development Corporation Limited

CORPORATE GOVERNANCE

CHURCHILL FALLS (LABRADOR) CORPORATION LIMITED

BRENDAN PADDICK
Chairperson
CEO, Columbus Capital Corp.

RICHARD CACCHIONE
President, Hydro-Québec Production

STELLA LENEY
Vice President Corporate Affairs and Corporate Secretary,
Hydro-Québec

JOHN GREEN
Lawyer, McInnes Cooper

STAN MARSHALL
President and CEO, Nalcor Energy

BOB WARR
Managing Director, Nor-Lab Limited

NALCOR ENERGY – OIL & GAS INC.

BRENDAN PADDICK
Chairperson
CEO, Columbus Capital Corp.

JUSTIN LADHA
Vice President, KMK Capital Inc.

MARK MACLEOD
President and CEO C-Core

STAN MARSHALL
President and CEO, Nalcor Energy

BRIAN MAYNARD
Retired Oil and Gas Executive

NALCOR ENERGY – BULL ARM FABRICATION INC.

EDNA TURPIN
Chairperson
Psychologist/Corporate Director

MARK MACLEOD
President and CEO, C-Core

STAN MARSHALL
President and CEO, Nalcor Energy

DEBBIE MOLLOY
Vice President, Corporate Services, Eastern Health

DAVID OAKE
President, Invenio Consulting Inc.

TWIN FALLS POWER CORPORATION LIMITED

CHRIS KIELEY
President
Vice President, Strategic Planning and Business Development,
Nalcor Energy

VAN ALEXOPOULOS
Director, Commercial Services, Iron Ore Company of Canada

ORAL BURRY
Manager, Safety, Health and Environment, CF(L)Co

ROBERT HULL
General Manager, Commercial Management and Integration,
Nalcor Energy

MAURICE MCCLURE
Vice President, Finance and Strategy,
Iron Ore Company of Canada

JIM MEANEY
Vice President, Finance, Power Supply, Nalcor Energy

MIKE ROBERTS
Chief Human Resources Officer and Vice President,
Safety, Health and Sustainability, Nalcor Energy

CORPORATE GOVERNANCE

LOWER CHURCHILL MANAGEMENT CORPORATION

JOHN MACISAAC
Chairperson
Executive Vice President, Power Supply, Nalcor Energy

GILBERT BENNETT
Executive Vice President, Power Development, Nalcor Energy

STAN MARSHALL
President and CEO, Nalcor Energy

JUNE PERRY
President and CEO, Pilot Communications

MIKE ROBERTS
Chief Human Resources Officer and Vice President,
Safety, Health and Sustainability, Nalcor Energy

LABRADOR-ISLAND LINK GENERAL PARTNER CORPORATION (General Partner of Labrador-Island Link Limited Partnership)

JOHN GREEN
Chairperson
Lawyer, McInnes Cooper

LIBBY BURNHAM
Lawyer

RON ELLSWORTH
Business Person

STAN MARSHALL
President and CEO, Nalcor Energy

EDNA TURPIN
Psychologist/Corporate Director

GEOFF GOODYEAR
Retired

LABRADOR-ISLAND LINK HOLDING CORPORATION

JACK HILLYARD
Chairperson
Retired BMO Executive

SHEILA KELLY-BLACKMORE
Business Person

JOHN MACISAAC
Executive Vice President, Power Supply, Nalcor Energy

DERRICK STURGE
Executive Vice President, Finance and Chief Financial Officer,
Nalcor Energy

BRENDAN PADDICK
CEO, Columbus Capital Corp.

LABRADOR-ISLAND LINK OPERATING CORPORATION

BRENDAN PADDICK
Chairperson
CEO, Columbus Capital Corp.

CHRISTOPHER HICKMAN
CEO, Marco Group of Companies

CHRIS LOOMIS
Professor (Retired)
Memorial University of Newfoundland

DAVID OAKE
President Invenio Consulting Inc.

DESMOND WHALEN
Medical Doctor, Faculty of Medicine
Memorial University of NL

GEOFF GOODYEAR
Retired

CORPORATE GOVERNANCE

LABRADOR TRANSMISSION CORPORATION

RONALD COLE
Chairperson
Lawyer, Cole Law Offices

JOHN MACISAAC
Executive Vice President, Power Supply, Nalcor Energy

STAN MARSHALL
President and CEO, Nalcor Energy

CHRIS WOODFORD
Architect, Woodford Sheppard Architecture

DERRICK STURGE
Executive Vice President, Finance and Chief Financial Officer,
Nalcor Energy

BRENDAN PADDICK
CEO, Columbus Capital Corp.

MUSKRAT FALLS CORPORATION

CHRISTOPHER HICKMAN
Chairperson
CEO, Marco Group of Companies

RICHARD DAW
Chartered Accountant

JACK HILLYARD
Retired BMO Executive

STAN MARSHALL
President and CEO, Nalcor Energy

JOHN QUAIKOE
Professor, Faculty of Engineering and Applied Science
Memorial University of Newfoundland

EDNA TURPIN
Psychologist/Corporate Director

NALCOR ENERGY MARKETING CORPORATION

BRIAN MAYNARD
Chairperson
Retired Oil and Gas Executive

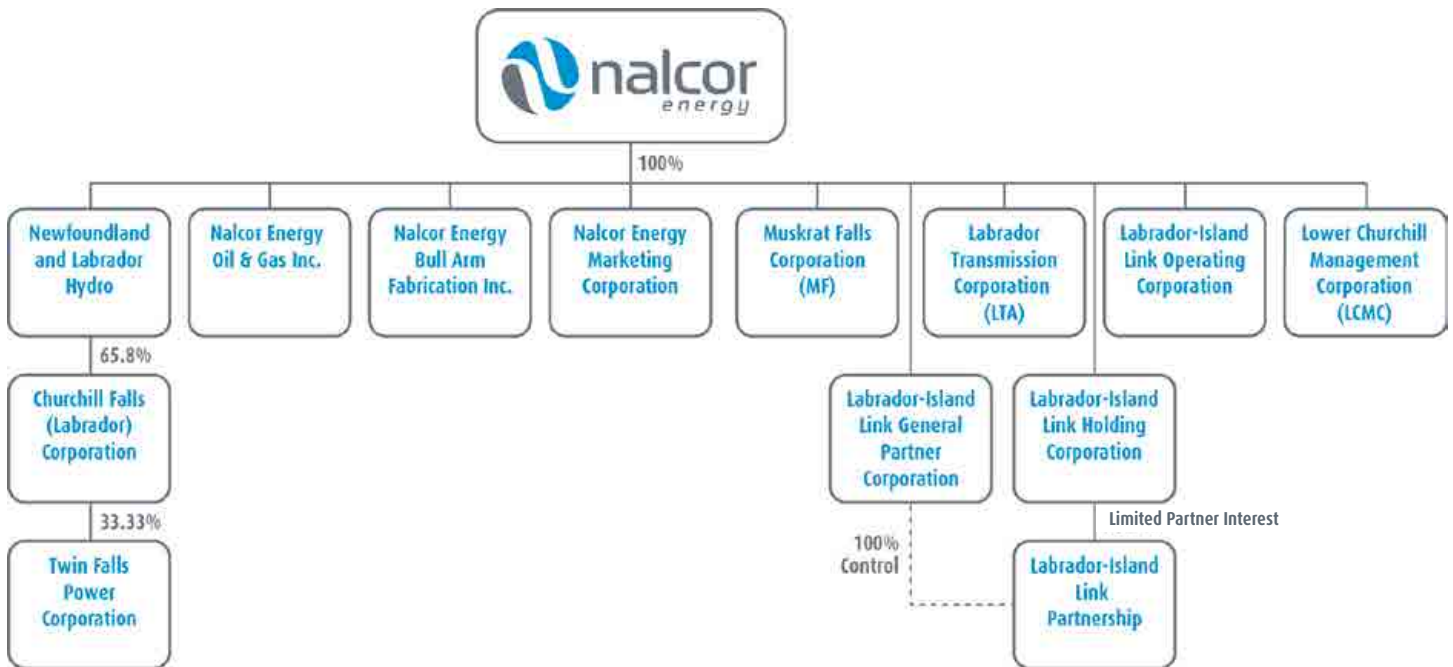
GREGORY CONNORS
Lawyer, McInnes Cooper

JOHN GREEN
Lawyer, McInnes Cooper

STAN MARSHALL
President and CEO, Nalcor Energy

DEBBIE MOLLOY
Vice President, Corporate Services, Eastern Health

CORPORATE GOVERNANCE



AUDIT COMMITTEE

The Audit Committee's primary duties and responsibilities are to:

- Serve as an independent and objective party to monitor the integrity of Nalcor's financial statements, financial reporting process and systems of internal controls regarding finance, accounting, and legal compliance;
- Identify and monitor the management of the principal risks that could impact the financial reporting of Nalcor;
- Appoint, approve compensation, and monitor the independence and performance of Nalcor's external auditors;
- Monitor the compliance by Nalcor with legal and regulatory requirements;
- Provide an avenue of communication among the external auditors, management, and the Board of Directors; and
- Encourage continuous improvement of, and foster adherence to, Nalcor's policies, procedures and practices at all levels.

CORPORATE GOVERNANCE

CORPORATE GOVERNANCE COMMITTEE

The Corporate Governance Committee's primary duties and responsibilities are to:

- a) Develop governance principles for Nalcor and its subsidiaries that are consistent with high standards of corporate governance and review and assess on an ongoing basis Nalcor's system of corporate governance;
- b) Identify and recommend candidates for appointment to the Nalcor Boards in the event of a vacancy;
- c) Review and recommend a process for Director orientation, assessment, and compensation; and
- d) Enterprise Risk Management with respect to Nalcor and its subsidiaries.

HUMAN RESOURCES AND COMPENSATION COMMITTEE

The Human Resources and Compensation Committee's primary duties and responsibilities are to:

- a) Establish and maintain a compensation philosophy and framework for Nalcor;
- b) Consider Nalcor's approach to and policies for recruiting, developing and motivating Executives and executive compensation and human resources issues;
- c) With the Chair of the Board of Directors, undertake an annual performance review of the President and CEO of Nalcor and report and/or make recommendations to the Board of Directors;
- d) Review and assess annually corporate performance metrics;
- e) Review and assess annually Nalcor's succession planning policies and practices for Executives, and report and/or make recommendations to the Board of Directors;
- f) Review the approach to employment diversity and inclusion;
- g) Review compliance with Nalcor's Code of Conduct; and
- h) Review Nalcor's labour relations strategies and recommend to the Board of Directors negotiating mandates for collective bargaining.

SAFETY, HEALTH, ENVIRONMENT AND COMMUNITY COMMITTEE

The Safety, Health, Environment and Community Committee's primary duties and responsibilities are to:

- a) Review and report to the Board of Directors on Nalcor's maintenance of safety, environment and health policies, procedures and practices and in the conduct of its operation, directed to prevent injury to its employees, the public and the environment;
- b) Review with Management whether Nalcor's safety, environment and health policies are being effectively implemented and in compliance with statutory and regulatory requirements;
- c) Review the findings of reports arising from internal and external audits and assessments of safety, environment and health issues, together with Management's response thereto and oversee to ensure that there is an agreed course of action leading to the resolution of any concerns, deficiencies or outstanding issues and timely follow-up on any unresolved matters;
- d) Review with Management the impact of proposed legislation in matters of safety, environment and health on the operations of Nalcor;
- e) Review and approve annually the safety and environmental audit plans by Nalcor and external auditors and review of annual Corporate safety performance and Corporate environmental report;
- f) Review with Management and make recommendations to the Board of Directors as appropriate on Nalcor's safety, environment, health and community programs, policies and procedures and any other matters relating to safety, environment, health and community that it considers relevant;
- g) Review with Management annually the three-year Corporate Reputation Plan and annual reputation priorities; and
- h) Meet with the Vice-President/Manager responsible at least annually to review safety, environmental, health or reputation matters that could have a material impact on Nalcor's reputation, business or financial position and report to the Board of Directors thereon in a timely manner.

CORPORATE GOVERNANCE

POLICY ON INDEPENDENCE OF EXTERNAL AUDITORS

The External Auditor Independence Policy is a policy governing Nalcor Energy and its subsidiaries' relationship with the External Auditor, including:

- a) establishing a process for determining whether various non-audit and other services provided by the External Auditor affects its independence;
- b) identifying the services that the External Auditor may and may not provide to Nalcor;
- c) pre-approving all services to be provided by the External Auditor; and
- d) establishing a process for hiring current or former members of the Audit Management Team of the External Auditor in a financial reporting oversight role to ensure auditor independence is maintained.

EXTERNAL AUDITOR'S FEES

The External Auditor of Nalcor and its subsidiaries is Deloitte. Deloitte has been the External Auditor since 2003. Professional fees incurred in 2017 in connection with audit and audit-related services were \$1.0 million (2016 - \$0.9 million) and fees related to non-audit services were \$nil (2016 - \$0.2 million).

ENERGY PORTFOLIO

LEGEND

- Hydroelectric Generation Station

- Thermal Plant/Combustion Turbine

- ▲ Diesel Plant

- ✈ Wind Generation

- ⚓ Offshore Oil Projects

- ★ Industrial Fabrication Site

- ◆ Diesel Plant operated on behalf of Mushuau Innu First Nation

* OPERATED UNDER LICENCE FROM THE GOVERNMENT OF NEWFOUNDLAND AND LABRADOR

PPA POWER PURCHASE AGREEMENT



APPENDIX 1



Table of Contents

02	Section 1: Corporate Overview
04	Section 2: Summary of Financial Highlights and Recent Developments
11	Section 3: Consolidated Financial Results
16	Section 4: Segmented Results and Analysis
28	Section 5: Liquidity and Capital Resources
35	Section 6: Key Business Risks
42	Section 7: Accounting Policies and Significant Accounting Judgments, Estimates and Assumptions
46	Section 8: Non-GAAP Financial Measures
47	Section 9: Related Party Transactions
48	Section 10: Summary of Quarterly Results
50	Section 11: Subsequent Event
51	Section 12: Outlook

HEAD OFFICE

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MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

SECTION 1: CORPORATE OVERVIEW

Nalcor Energy (Nalcor or the Company) is Newfoundland and Labrador's energy company. Nalcor is a Crown corporation established in 2007 under a special act of the Legislature of the Province of Newfoundland and Labrador (the Province). The company's business includes the development, generation, transmission and sale of electricity; the exploration, development, production and sale of oil and gas; industrial fabrication site management; and energy trading.

Nalcor's legal structure as at December 31, 2017 included the entities listed below:

Entity Name	Description of Interest
Newfoundland and Labrador Hydro (Hydro)	Wholly owned subsidiary
Nalcor Energy – Oil and Gas Inc. (Oil and Gas)	Wholly owned subsidiary
Nalcor Energy – Bull Arm Fabrication Inc. (Bull Arm Fabrication)	Wholly owned subsidiary
Nalcor Energy Marketing Corporation (Energy Marketing)	Wholly owned subsidiary
Muskrat Falls Corporation (Muskrat Falls) ¹	Wholly owned subsidiary
Labrador Transmission Corporation (Labrador Transco) ¹	Wholly owned subsidiary
Labrador-Island Link Holding Corporation (LIL Holdco) ¹	Wholly owned subsidiary
Labrador-Island Link General Partner Corporation (LIL GP) ¹	Wholly owned subsidiary
Labrador-Island Link Operating Corporation (LIL OpCo) ¹	Wholly owned subsidiary
Lower Churchill Management Corporation (LCMC) ¹	Wholly owned subsidiary
Churchill Falls (Labrador) Corporation Limited (Churchill Falls)	65.8% owned joint operation of Hydro
Twin Falls Power Corporation Limited (Twin Falls)	33.3% owned joint venture of Churchill Falls
Labrador-Island Link Limited Partnership (LIL LP) ¹	Limited partnership in which Nalcor, through LIL Holdco, owns 100% of the 75 Class A, 1 Class C limited partnership units and 1 General Partner Unit
Gull Island Power Corporation (GIPCo)	Wholly owned subsidiary (inactive)
Lower Churchill Development Corporation (LCDC)	51% owned subsidiary of Hydro (inactive)

¹ These entities comprise the Lower Churchill Project (LCP)

The operating structure as at December 31, 2017 reflects organizational changes that resulted in revised operating segments effective January 1, 2017. The designation of segments is based on a combination of regulatory status and management accountability. Previously reported segmented information has been presented to conform with the current operating structure. The following summary provides a brief overview of the nature of the operations included in each of the Company's six business segments.

Hydro – is comprised of both regulated and non-regulated activities.

- **Hydro Regulated** activities encompass sales of electricity to customers within the Province that are regulated by the Newfoundland and Labrador Board of Commissioners of Public Utilities (PUB).
- **Hydro Non-Regulated** activities include the sale of power, purchased from Churchill Falls, to mining operations in Labrador West as well as costs related to operations that Hydro manages that are not subject to rate regulation by the PUB.

Power Development - includes the development activities of the 824 MW **Muskrat Falls** hydroelectric generating facility currently under construction in Labrador on the Lower Churchill River. Once construction is complete this asset and its operating results will become part of the Power Supply segment.

Power Supply – is comprised of the following:

- **LCP Transmission** includes the construction and operation of the Labrador-Island Link (LIL) and Labrador Transmission Assets (LTA), which consists of transmission lines connecting the Muskrat Falls hydroelectric plant, the Churchill Falls hydroelectric facility, and certain portions of the transmission system in Labrador to the island of Newfoundland.
- **Churchill Falls** owns and operates a hydroelectric generating facility which sells electricity to Hydro-Québec and Hydro.
- **Other** includes revenues and costs recovered from Hydro-Québec associated with Nalcor's operation of the Menihek Generating Station, the Maritime Link (which is owned by Emera, but consolidated by Nalcor), administration and community development costs related to Power Supply, and costs associated with the management of LCP construction.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Energy Markets - includes energy trading activities and commercial activities related to the development of energy markets.

- **Energy Trading** includes the sale of available excess energy, primarily Recapture, to export markets in eastern Canada and the northeastern United States. Recapture refers to excess energy from the 300 MW block of electricity which Churchill Falls has agreed to sell and deliver to Hydro to service its residential, commercial and industrial Labrador Interconnected customers.
- **Commercial and Other** includes costs associated with Gull Island and business development activities related to exploring additional markets and sources for future energy generation and transmission.

Offshore Development - includes the following:

- **Oil and Gas** activities include Nalcor's share of exploration, development, production, transportation and processing sectors of the oil and gas industry.
- **Bull Arm Fabrication** consists of an industrial fabrication site which is subleased to third parties.

Corporate - includes corporate support and shared services functions.

Nalcor maintains appropriate systems of internal control, policies and procedures which provide Management with reasonable assurance that assets are safeguarded and its financial information is reliable. The following discussion and analysis includes results as of December 31, 2017 with subsequent event and outlook information updated up to March 2, 2018. The Management's Discussion and Analysis (MD&A) is the responsibility of Management and the Board of Directors carries out its responsibility for review of this disclosure principally through its Audit Committee. This MD&A was reviewed by the Audit Committee and approved by the Board of Directors on March 2, 2018.

This MD&A should be read in conjunction with the annual audited consolidated financial statements of Nalcor for the year ended December 31, 2017.

Basis of Presentation

Unless otherwise noted, all financial information has been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board.

All financial information is reported in Canadian dollars (CAD), unless otherwise noted.

Non-GAAP Financial Measures

Certain financial measures in this MD&A are not prescribed by IFRS as contained within Part I of the Chartered Professional Accountants of Canada Handbook. These non-generally accepted accounting principles (Non-GAAP) financial measures are defined in Section 8 - Non-GAAP Financial Measures.

Forward-Looking Information

Certain statements in this MD&A are forward-looking statements, based on Nalcor's current expectations, estimates, projections and assumptions, which are subject to risks and uncertainties. Statements containing words such as "could", "should", "will", "expect", "may", "anticipate", "believe", "intend", "estimate", "budget", "forecast", "plan" and similar expressions constitute forward-looking statements. By their nature, forward-looking statements require Management to make assumptions and are subject to important unknown risks and uncertainties, which may cause actual results in future periods to differ materially from forecasted results. While Management considers these assumptions to be reasonable and appropriate based on information currently available, there is a risk that they may not be accurate. Nalcor assumes no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or any other reason.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

SECTION 2: SUMMARY OF FINANCIAL RESULTS AND RECENT DEVELOPMENTS

FINANCIAL HIGHLIGHTS

Key Profit Drivers

Key profit drivers vary across each of Nalcor's business segments as there are a combination of regulated operations, operations with long-term and medium-term supply contracts and operations in markets where revenues are driven entirely by commodity prices (export electricity and oil). Nalcor's profitability is also impacted by exchange rate fluctuations for a number of foreign currencies, the most significant being the CAD/United States Dollar (USD) exchange rate. Nearly all revenue generated by Oil and Gas, Energy Trading and Bull Arm Fabrication is denominated in USD. Short-term volatility is partially mitigated through USD hedging. However, in general, any fluctuations in the USD exchange rate have a direct impact on Nalcor's profit. Various expenses, capital expenditures and Statement of Financial Position balances include amounts denominated in USD, particularly Hydro Regulated's fuel purchases for the Holyrood Thermal Generating Station (HTGS). Cost variances for these fuel purchases as a result of exchange rate fluctuations are captured in the Rate Stabilization Plan (RSP) and do not impact Nalcor's profit.

Hydro Regulated is entitled to the opportunity to recover, through customer rates, all reasonable and prudent costs incurred in providing electricity service to its customers, in addition to a just and reasonable return on rate base, in accordance with Section 80 of the Public Utilities Act. Failure to obtain rate orders on a timely basis as applied for may adversely affect the profit of Hydro Regulated.

Certain costs incurred during the construction of LCP assets are not eligible for capitalization under IFRS, including costs related to components of assets being brought into service in advance of full project commissioning. As a result, until the financing and legislative arrangements that allow for the recovery of LCP costs come into effect, these costs will directly impact Nalcor's profit and may be material. These costs will be recovered in future reporting periods through rates in Hydro Regulated. As well, with the LTA and LIL assets moving from the development to testing / operational phase, there will be material interest and operating costs recognized in profit or loss starting in 2018 before the full project comes into service. Hydro Regulated has filed for a deferral account in its General Rate Application (GRA or Application) with respect to the operating costs associated with these assets pre-commissioning. This matter remains before the PUB. Hydro Regulated is determining its approach to filing an application with the PUB in 2018 to defer the recognition of interest costs associated with LIL and LTA and to defer collection of them until all the LCP assets are in-service. In the absence of a deferral account, these expenses will have an impact on profit or loss.

Nalcor may incur impairment expenses and future reversal of such expenses due to changes in discounted projected future cash flows when compared to the carrying values of related assets. Any expense or reversal of such expense is reflected in Nalcor's results, and while no impact on cash flows, can lead to large fluctuations in profit or loss between financial reporting periods.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	2015	2017	2016	2015
Revenue	265	227	219	930	824	811
Operating profit ¹	38	62	25	169	136	46
(Loss) profit	(94)	62	(36)	63	136	(16)
Funds from operations (FFO) ¹	86	103	56	370	279	149
Earnings before interest, taxes, depreciation, depletion, amortization, impairment and accretion (EBITDA) ¹	100	117	73	429	343	217
Return on capital employed (ROCE) ^{1,2}				7.2%	7.9%	4.5%
Capital expenditures ³	673	761	693	2,836	2,801	2,462
Oil production (thousands of bbls)	809	733	225	3,235	2,226	525
Realized oil price (CAD/bbl)	80	69	71	70	64	83
Electricity sales (GWh):						
Regulated	2,076	2,032	2,085	7,626	7,461	7,671
Export sales - Hydro-Québec	7,302	7,302	8,099	28,970	27,995	28,692
Export - other markets	359	378	373	1,594	1,627	1,569
Realized electricity price - Other Export Markets (CAD/MWh)	37	30	32	31	30	37

¹See Section 8 - Non-GAAP Financial Measures

²Rolling 12 month average

³Excluding Maritime Link

Profit

Nalcor's loss for the three months ended December 31, 2017 was \$94 million compared to a \$62 million profit for the same period in 2016, a decrease of \$156 million. Key drivers of the decrease include impairment expenses related to exploration intangible assets as well as Gull Island Project costs; an increase in operating costs primarily related to the Community Development Agreement (CDA) signed between Nalcor and the NunatuKavut Community Council to provide direct investment to Southern Inuit and communities; an increase in depreciation and depletion in Hydro Regulated and Oil and Gas; losses on disposal of assets in Oil and Gas associated with the conclusion of Hebron construction; increased production, marketing and transportation costs in Oil and Gas; and the impact of timing of the recognition of 2016 cost deferrals in Hydro Regulated. The decrease was partially offset by higher oil revenue due to increases in volume and average Dated Brent prices.

Nalcor's profit for the year ended December 31, 2017 was \$63 million compared to \$136 million for the same period in 2016, a decrease of \$73 million. Key drivers of the decrease include impairment expenses related to exploration intangible assets as well as Gull Island Project costs; higher depletion associated with increased production in Oil and Gas; losses on disposal of assets in Oil and Gas associated with the conclusion of Hebron construction; losses on settlement of oil commodity contracts compared to prior year gains in Oil and Gas; increased production, marketing and transportation costs in Oil and Gas; higher depreciation and amortization in Hydro Regulated and Oil and Gas; and increased operating costs as a result of the CDA and higher costs associated with salaries and benefits, system equipment maintenance and insurance. The decrease was partially offset by higher oil revenue as a result of increased production and higher oil prices; the recognition of a one-time adjustment to the Bull Arm Fabrication lease revenue related to the close-out value of the ExxonMobil Canada Properties (EMCP) sublease agreement; higher capitalized interest; increased revenue in Hydro Regulated due to higher demand; and the impact of timing and recognition of cost deferrals in Hydro Regulated.

A detailed discussion of the performance of each of Nalcor's segments is contained in Section 4 - Segmented Results and Analysis.

FFO and EBITDA

FFO for the three months ended December 31, 2017 were \$86 million compared to \$103 million for the same period in 2016, a decrease of \$17 million. FFO for the year ended December 31, 2017 were \$370 million compared to \$279 million for the same period in 2016, an increase of \$91 million.

EBITDA for the three months ended December 31, 2017 was \$100 million compared to \$117 million for the same period in 2016, a decrease of \$17 million. EBITDA for the year ended December 31, 2017 was \$429 million compared to \$343 million for the same period in 2016, an increase of \$86 million.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

The decrease and increase in these metrics for the quarter and year, respectively, was primarily due to the drivers noted in the profit analysis above.

ROCE

ROCE for the year ended December 31, 2017 was 7.2% compared to 7.9% for the same period in 2016, a decrease of 0.7%. The decrease primarily relates to higher average capital employed as a result of higher debt in Hydro Regulated and increases in equity; partially offset by increased operating profit as a result of the drivers noted above, excluding impairment and the Bull Arm lease settlement.

Capital Expenditures

Capital expenditures for the year ended December 31, 2017, excluding Maritime Link, of \$2,836 million were \$35 million higher than the same period in 2016, primarily due to increases in capital incurred in Muskrat Falls and Hydro Regulated, partially offset by decreases in capital for LCP Transmission and Oil and Gas. A detailed discussion of the segmented capital expenditures is provided in Section 5 - Liquidity and Capital Resources.

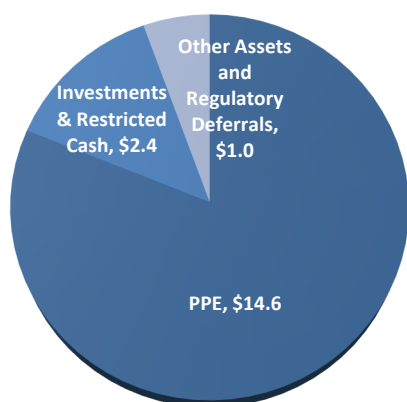
Statement of Financial Position

As at December 31 (millions of dollars)

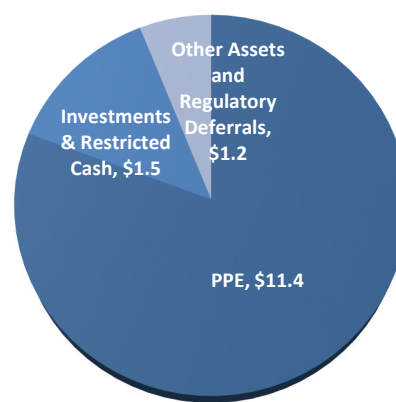
	2017	2016	2015
Total assets	18,034	14,063	12,322
Capital assets, net	14,554	11,417	8,325
Total debt (net of sinking funds)	10,063	6,583	6,303
Shareholder's equity	5,081	4,264	3,475
Debt to capital (%)	66%	61%	65%

Total Assets

December 31, 2017 - \$18.0 billion



December 31, 2016 - \$14.1 billion



Nalcor's total assets as at December 31, 2017 were \$18.0 billion, compared to \$14.1 billion as at December 31, 2016, primarily due to proceeds from the issuance of \$2.9 billion additional debt in Muskrat Falls and LCP Transmission and capital expenditures. The composition of the Company's assets as at December 31, 2017 included property, plant and equipment (PPE) of \$14.6 billion (December 31, 2016 - \$11.4 billion), investments and restricted cash primarily from the proceeds of the Muskrat Falls and LCP Transmission financing of \$2.4 billion (December 31, 2016 - \$1.5 billion), and other assets and regulatory deferrals totaling \$1.0 billion (December 31, 2016 - \$1.2 billion).

Total Liabilities and Equity

Total liabilities at December 31, 2017 were \$12.9 billion compared to \$9.5 billion at December 31, 2016, an increase of \$3.4 billion. This increase is primarily due to the issuance of \$2.9 billion additional debt in Muskrat Falls and LCP Transmission.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Equity as at December 31, 2017 was \$5.1 billion compared to \$4.3 billion at December 31, 2016, an increase of \$0.8 billion. This increase is primarily due to additional equity contributions from the Government of Newfoundland and Labrador (the Shareholder or the Province) and profit during the year, partially offset by other comprehensive losses during the year associated with the cash flow hedges that were entered into as a result of the Muskrat Falls and LCP Transmission additional debt issue during Q2 2017.

Further details on changes in the Consolidated Statement of Financial Position are included in Section 3 – Consolidated Financial Results.

Debt to Capital

Debt to capital increased to 66% for the year ended December 31, 2017 compared to 61% at December 31, 2016, primarily due to the issuance of \$2.9 billion additional debt in Muskrat Falls and LCP Transmission during Q2 2017. See Section 5 – Liquidity and Capital Resources for further details.

RECENT DEVELOPMENTS

HYDRO REGULATED

2017 General Rate Application

Hydro Regulated filed its 2017 GRA in July 2017, using 2018 and 2019 Test Years. The 2017 GRA requested interim rates effective January 1, 2018 and final rates effective January 1, 2019. If Hydro Regulated's Application is approved, rates will increase on average by 6.6% in 2018 and 6.4% in 2019 for residential customers on the island; by 4.4% in 2018 and 8.2% in 2019 for interconnected system customers in Labrador; and by 6.3% in 2018 and 7.1% in 2019 for island industrial customers. Due to a delay in the interim rate process, interim rates were not in place by January 1, 2018. The recovery of the requested revenue requirement for the period in 2018, while existing rates remain in effect, will be addressed through the 2017 GRA process in 2018. The intervenors for Hydro Regulated's 2017 GRA are Newfoundland Power, the Consumer Advocate, the Island Industrial Customer Group, the Labrador Interconnected Group, and the Iron Ore Company of Canada.

During the fourth quarter, Hydro Regulated received and responded to in excess of 950 requests for information (RFI) and filed expert evidence in support of its Application. The public hearing portion of the 2017 GRA was scheduled to begin on January 30, 2018, however, was delayed due to an application by the Consumer Advocate requesting additional information. Settlement proceedings occurred at the end of February and Hydro is currently working to provide further information requested during these sessions. The hearing has been rescheduled to commence in April 2018.

2013 General Rate Application

In December 2016, Hydro Regulated received Board Order No. P.U. 49(2016) (the 2013 GRA Order). Hydro Regulated filed compliance applications in January and May of 2017 to address the items in the 2013 GRA Order, which were ruled on by the PUB in Board Order No. P.U. 22(2017) (the Compliance Order). The PUB then issued a series of orders that resulted in new rates for both Hydro Regulated and Newfoundland Power's customers that were effective July 1, 2017, which concluded the 2013 GRA. As part of the final Order, the PUB approved new supply cost deferral accounts effective January 1, 2015. Hydro Regulated anticipates filing its application for approval of amounts to be recovered from these deferral accounts in Q1 2018, with recovery subject to a future Board Order. The impact of all orders associated with the 2013 GRA has been reflected in the 2017 financial results.

2017 RSP

On July 1, 2017, Hydro Regulated also implemented a rate change in accordance with the normal operation of the RSP. This rate change included a revised No. 6 fuel rider to reflect an increase in forecasted fuel price, a revised RSP Current Plan rider, and a RSP rate mitigation adjustment as ordered by the PUB. The RSP rate mitigation adjustment utilized approximately \$55 million in past fuel savings in the RSP to reduce the July 1, 2017 rate increase to customers. The RSP rate mitigation adjustment is scheduled to expire on July 1, 2018.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

RSP Surplus Refund

In July 2016, Hydro Regulated filed an application with the PUB for approval of a plan to refund the balance in the RSP Surplus to Newfoundland Power and Hydro Regulated's Island Interconnected Rural customers. Newfoundland Power also filed an application to refund their portion of the RSP Surplus balance to their customers. The RSP Surplus to be refunded was approximately \$141 million. The PUB approved both applications.

Refunds began in the first quarter of 2017. At the end of Q4 2017, approximately \$131 million, or 93% of the balance due has been refunded.

2018 Capital Budget

On July 28, 2017, Hydro Regulated filed its 2018 Capital Budget Application seeking approval for \$206.2 million. The application was subsequently reduced to \$198.9 million as a result of revised estimates for one project and the withdrawal of another project due to new information. RFIs were received and responses provided in September 2017. The PUB issued Board Order No. P.U. 43(2017) approving \$170.9 million of the proposed budget, deferring its decision on two projects, pending additional information to be submitted to the PUB. Hydro Regulated submitted this information in January 2018, and expects a decision in early 2018.

2017 Supplemental Capital

Hydro Regulated filed and received approval for seven supplemental capital applications and three emergency capital projects during 2017, totaling approximately \$30.5 million.

Investigation and Hearing into Supply Issues and Power Outages – Phase II

The Phase II investigation and hearing into supply issues and power outages on the Island Interconnected System, which began in January 2014, is ongoing. The focus of this proceeding continues to be on the reliability and adequacy of the Island Interconnected System leading up to, and after, the interconnection of Muskrat Falls.

In January 2017, the PUB engaged Liberty Consulting (Liberty) to provide a report to determine whether there were any immediate steps necessary to reduce the risks to the adequate and reliable supply on the Island Interconnected System as currently configured and to develop a preliminary list of issues which should be addressed to assess adequacy and reliability on the Island Interconnected System upon interconnection.

Liberty provided recommendations in its report on the first matter on February 27, 2017 and concluded that based on the information at that time, Hydro Regulated could demonstrate adequate and reliable supply pre-Muskrat Falls without acquiring additional capacity. On April 13, 2017, Hydro Regulated filed its response to Liberty's report agreeing with Liberty's recommendations and provided proposed actions and timelines to address the recommendations. The PUB agreed with Liberty's report and set additional quarterly reporting requirements for Hydro Regulated to continue to monitor Hydro Regulated's progress.

In May 2017, the PUB established an issues list setting out the critical remaining information to be provided by Hydro Regulated in relation to these issues. By August 2017, Hydro Regulated had responded to all requests for information.

On August 16, 2017, the PUB engaged Liberty to assist in determining a monitoring framework to track the progress of the integration of the Muskrat Falls, Labrador-Island Link and Maritime Link assets into the Island Interconnected System. Meetings were held between Liberty and Hydro Regulated and it was determined that Hydro Regulated will provide Liberty with a fourth quarter progress update in Q1 2018.

During Q4 2017, Hydro Regulated filed the final two of its three 2017-2018 Winter Readiness Planning reports and subsequently provided a further update on items in the report, as requested by the PUB.

Other Regulatory Activity

On November 21, 2017, Hydro Regulated filed an application for approval to issue debt in the aggregate not to exceed \$700 million on or before March 31, 2018, pursuant to Section 91 of the Public Utilities Act. Hydro Regulated's application was approved in Board Order No. P.U. 42(2017).

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

CHURCHILL FALLS

The initial term of the 1969 Power Contract between Churchill Falls and Hydro-Québec expired in 2016. A Renewal Contract commenced September 1, 2016 and resulted in a decrease in the contract rate from 2.5426 mills per kWh to 2.0 mills per kWh as well as a change in the contract methodology from revenue recognition based upon the energy delivered to Hydro-Québec to revenue recognition based upon an interim Annual Energy Base agreed upon by both parties, which can differ from energy delivered. The Renewal Contract expires on August 31, 2041 and since 2017 was the first full year of the Renewal Contract, revenue for Churchill Falls is lower compared to prior year.

In August 2016, Churchill Falls received judgment from the Québec Court of Appeal upholding the 2014 Québec Superior Court ruling on the motion filed by Churchill Falls to address the inequities of the pricing terms of the 1969 Power Contract between Churchill Falls and Hydro-Québec. The Court ruled against Churchill Falls. In April 2017, Churchill Falls was granted leave to appeal the case to the Supreme Court of Canada. The case was presented in December 2017 and a final ruling is anticipated some time in 2018.

Also in August 2016, Churchill Falls received judgment from the Québec Superior Court regarding a Motion for Declaratory Judgment filed by Hydro-Québec relating to the interpretation of the 1969 Power Contract between Churchill Falls and Hydro-Québec and the associated Renewal Contract. The Court ruled in favour of Hydro-Québec. Churchill Falls has filed a Notice of Appeal with the Québec Court of Appeal. The date of the appeal hearing has not yet been set but it is anticipated that it will be scheduled for some time in 2018.

OTHER POWER SUPPLY

During December 2017, Emera NL, Hydro Regulated and Nova Scotia Power facilitated the first flow of electricity across the Maritime Link between the Province and Nova Scotia. This was part of commissioning activities that continued throughout the month, as the Maritime Link prepares to be ready for use in early 2018. It is expected that the Maritime Link will be available, in early 2018, to Hydro Regulated for delivery of off-island energy purchases to reduce the consumption of fuel at Holyrood.

MUSKRAT FALLS AND LCP TRANSMISSION

On May 25, 2017, Muskrat Falls and LCP Transmission received additional debt proceeds of \$2.9 billion for purposes of funding the remaining construction costs of the Muskrat Falls generating facility, the LTA and the LIL. The debt carries a direct, absolute, unconditional and irrevocable guarantee from Canada, and thereby carries an AAA credit rating or equivalent. In exchange for the proceeds, 138 series bonds were issued with interest rates ranging from 1.14% to 2.86%, maturing every six months beginning in December 2020. In May 2017, LCP Transmission and Muskrat Falls entered into six bond forward contracts totaling \$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 decrease in fair value of \$67 million was recorded between other comprehensive (loss) income and other expense (income), \$65.9 million and \$1.1 million, respectively. On July 27, 2017, Muskrat Falls and LCP Transmission purchased six structured deposit notes in the amount of \$2.1 billion using proceeds from the \$2.9 billion debt issue in May 2017. The deposit note investments are restricted in nature and subject to the provisions contained within the Project Finance Agreements.

On June 22, 2017, Nalcor provided an update on LCP, including the current projected schedule and expected costs for the hydroelectric development, transmission lines and associated infrastructure. The facilities capital cost forecast for the project is currently estimated at \$10.1 billion, along with financing and other costs of \$2.6 billion, for a total of \$12.7 billion.

Commissioning activities related to the Maritime Link commenced in December 2017. The Maritime Link, LIL and LTA are each expected to be available, in limited capacity, to Hydro Regulated for delivery of off-island energy purchases to reduce the consumption of fuel at Holyrood.

Commission of Inquiry into the Muskrat Falls Project

On July 24, 2017, Nalcor received written notice from the Province that an investigation regarding the development of LCP was forthcoming. On November 20, 2017, the Province released details establishing the Terms of Reference for the Commission of Inquiry into the Muskrat Falls Project ("the Inquiry"). The Inquiry is expected to be ongoing for two years, with the final report due December 31, 2019.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

ENERGY TRADING

Energy Trading has been completing readiness activities in advance of the completion of the Maritime Link, LTA and LIL in 2018. Late in 2017, Energy Trading executed a short-term agreement with Hydro Regulated to facilitate energy imports for the purpose of fuel displacement at the HTGS. Energy Trading also completed recruitment of water management and production scheduling staff with a primary focus on optimizing the value of Nalcor's electricity assets and its participation in extra-provincial electricity markets following the interconnection of the island to the North American electricity grid.

OIL AND GAS

The White Rose (WR) Wellhead Platform Project was sanctioned in Q2 2017 with Oil and Gas holding a 5% interest in the WR Extension portion of the project. Oil and Gas' capital spend associated with the Wellhead Platform Project is anticipated to be approximately \$115 million to first oil in late 2022.

The Hebron Project reached significant milestones in 2017, with the tow to field of the platform in June and first oil on November 27, 2017.

BULL ARM FABRICATION

In June 2017, Bull Arm Fabrication finalized the close-out value of the ExxonMobil Canada Properties (EMCP) multi-year sublease agreement and recorded a one-time adjustment to lease revenue of approximately \$26 million. Site tenancy by EMCP concluded in December 2017 following completion of the Hebron Project.

In October 2017, Nalcor Energy issued a Request for Proposals (RFP) to assess proposed use for the Bull Arm Fabrication site following EMCP's demobilization. Four proposals have been received and are being evaluated with the goal of securing a tenant in the near future.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

SECTION 3: CONSOLIDATED FINANCIAL RESULTS

CONSOLIDATED STATEMENT OF PROFIT AND COMPREHENSIVE INCOME HIGHLIGHTS

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Revenue	265	227	38	930	824	106
Fuels	80	50	30	226	168	58
Power purchased	14	15	(1)	62	61	1
Operating costs	62	53	9	219	207	12
Production, marketing and transportation costs	13	8	5	36	26	10
Transmission rental and market fees	6	5	1	25	22	3
Depreciation, depletion, amortization and impairment	178	38	140	300	135	165
Exploration and evaluation	1	2	(1)	1	2	(1)
Net finance expense	16	16	-	66	72	(6)
Other expense (income)	7	5	2	23	(4)	27
(Loss) profit before regulatory adjustments	(112)	35	(147)	(28)	135	(163)
Regulatory adjustments	(18)	(27)	9	(91)	(1)	(90)
(Loss) profit for the period	(94)	62	(156)	63	136	(73)
Other comprehensive loss for the period	(3)	(8)	5	(78)	(5)	(73)
Total comprehensive (loss) income for the period	(97)	54	(151)	(15)	131	(146)

Non-GAAP Operating Profit Disclosure

Reconciliation of Nalcor's (loss) profit to operating profit for the three and twelve months ended December 31 is as follows:

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
(Loss) profit for the period	(94)	62	(156)	63	136	(73)
Impairment of property, plant and equipment	51	-	51	51	-	51
Impairment of exploration intangible assets	81	-	81	81	-	81
Close-out of Hebron sublease agreement	-	-	-	(26)	-	(26)
Operating profit for the period	38	62	(24)	169	136	33

Revenue

Revenue for the three months ended December 31, 2017 was \$265 million compared to \$227 million for the same period in 2016, an increase of \$38 million. Revenue for the year ended December 31, 2017 was \$930 million compared to \$824 million, an increase of \$106 million. The increase for the quarter was primarily due to an increase in Hydro Regulated revenue as a result of the normal operation of the RSP, which reflected higher fuel prices in the second half of 2017; increased rural revenue; increased revenue from Newfoundland Power, largely due to higher energy volumes; and increased revenue in Oil and Gas due to an increase in average Dated Brent price per barrel as compared to the same period in 2016, along with an increase in production volumes.

The increase in revenue for the year was primarily due to an increase in Oil and Gas revenue as a result of higher average Dated Brent oil prices and an increase in production volumes, as well as the recognition of a one-time adjustment to Bull Arm Fabrication lease revenue related to the close-out value of the EMCP sublease agreement.

Fuels

Fuel costs for the three months ended December 31, 2017 were \$80 million compared to \$50 million for the same period in 2016, an increase of \$30 million. The increase for the quarter was primarily due to an increase in both No. 6 fuel price and volume.

Fuel costs for the year ended December 31, 2017 were \$226 million compared to \$168 million for the same period in 2016, an increase of \$58 million. The increase for the year was primarily due to increases in No. 6 fuel and gas turbine fuel prices. This increase was partially offset by a decrease in gas turbine fuel volume.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

The majority of variances in fuel are either offset through the RSP or through other regulatory mechanisms in the regulatory adjustments line.

Power purchased

Power purchased for the three months and year ended December 31, 2017 was comparable to the same periods in 2016.

Operating costs

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Salaries and benefits	31	26	5	135	130	5
Maintenance and materials	12	12	-	39	35	4
Professional services	5	5	-	15	18	(3)
Insurance	2	2	-	7	6	1
Travel and transportation	1	2	(1)	7	6	1
Advertising, donations and community involvement	8	-	8	10	1	9
Rental and royalty	1	2	(1)	4	5	(1)
Other operating costs	2	4	(2)	2	6	(4)
Total operating costs	62	53	9	219	207	12

Operating costs for the three months ended December 31, 2017 were \$62 million compared to \$53 million for the same period in 2016, an increase of \$9 million. Operating costs for the year ended December 31, 2017 were \$219 million compared to \$207 million for the same period in 2016, an increase of \$12 million. The increase in operating costs for the quarter was primarily due to costs incurred as part of the CDA and increased salaries and benefits, partially offset by lower bad debt expense in 2017.

The increase in operating costs for the year primarily relates to CDA costs and increases in salaries and benefits, maintenance and materials, partially offset by a reduction in professional services and bad debt expense.

Production, marketing and transportation costs

Oil and Gas' production, marketing and transportation costs for the three months ended December 31, 2017 were \$13 million compared to \$8 million for the same period in 2016, an increase of \$5 million. Production, marketing and transportation costs for the year ended December 31, 2017 were \$36 million compared to \$26 million for the same period in 2016, an increase of \$10 million. The increase for the quarter and year was primarily due to an increase in production volumes and increased project operating costs associated with Oil and Gas' joint venture projects.

Transmission rental and market fees

Energy Trading's transmission rental and market fees for the three months ended December 31, 2017 were comparable to the same period in 2016. Transmission rental and market fees for the year ended 2017 were \$25 million compared to \$22 million in 2016, an increase of \$3 million due to an increase in transmission purchased to deliver energy to export markets and an increase in firm transmission rates compared to 2016.

Depreciation, depletion, amortization and impairment

Depreciation, depletion, amortization and impairment for the three months ended December 31, 2017 was \$178 million compared to \$38 million for the same period in 2016, an increase of \$140 million. Depreciation, depletion, amortization and impairment for the year ended December 31, 2017 was \$300 million compared to \$135 million for the same period in 2016, an increase of \$165 million. The increase for the quarter and year was primarily due to impairment expenses related to exploration intangible assets and previously capitalized Gull Island costs; an increase in Oil and Gas depletion associated with higher production volumes; and increased levels of investment in property, plant and equipment in Hydro Regulated.

With respect to the impairment of Gull Island, the assessment included reviewing older costs that no longer contribute to the future economic value of the project due to the passage of time. The majority of costs included as part of the impairment were incurred prior to 2005 and related to commercial, financing and other related activities. Nalcor continues to carry capitalized costs of \$140 million related

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

to environmental assessments, impact and benefits agreement, engineering, commercial, and related activities which management believes have future value towards the project.

The exploration program has been successful in making data available, attracting new participants to the NL offshore, supporting increased land sales, and identification of previously unknown prospects. This work has generally provided benefits to the Province and the future development of the oil and gas industry. However, because of the time horizon required to bring a project to the development stage, the period for Nalcor to realize a return on its investment is some considerable number of years away. Nalcor had previously been amortizing each exploration program over a six year period. In 2017 Nalcor made the decision to write down the balance of the unamortized exploration costs. The resulting impact was reducing 2017 profit, but will result in no amortization in future years.

Net finance expense

Net finance expense for the three months ended December 31, 2017 was comparable to the same period in 2016. Net finance expense for the year ended December 31, 2017 was \$66 million compared to \$72 million for the same period in 2016, a decrease of \$6 million. The decrease for the year was primarily due to higher capitalized interest related to an increase in Hydro Regulated's capital program and reduced interest resulting from the retirement of Hydro Regulated's long-term debt in 2016 that was refinanced during 2017 at lower interest rates. These decreases were partially offset by higher short-term borrowing levels and lower income associated with sinking funds as a result of the repayment of Hydro Regulated's Series X debentures.

Other expense (income)

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Settlement of commodity swaps	2	(1)	3	2	(10)	12
Settlement of foreign exchange forwards	(1)	-	(1)	(1)	-	(1)
Loss on disposal of property, plant and equipment	12	6	6	20	7	13
Foreign exchange (gain) loss	(4)	(1)	(3)	3	1	2
Other operating costs	(2)	1	(3)	(1)	(2)	1
Total other expense (income)	7	5	2	23	(4)	27

Other expense for the three months ended December 31, 2017 was comparable to the same period in 2016. Other expense for the year ended December 31, 2017 was \$23 million compared to other income of \$4 million for the same period in 2016, an increase in expense of \$27 million.

The increase in expense for the year was primarily related to an increase in losses associated with the disposal of assets and settlements related to commodity contracts.

Regulatory adjustments

Regulatory recoveries for the three months ended December 31, 2017 of \$18 million were lower than recoveries of \$27 million for the same period in 2016, a decrease of \$9 million. The variance in the quarter was primarily due to the approval of the 2016 cost deferral in Q4 2016 and RSP amortization. This was partially offset by: RSP deferred fuel costs as a result of the normal operation of the RSP; reduced RSP interest due to lower RSP balances; adjustments for amounts related to the 2014-2015 cost deferral accounts recognized in Q4 2016 associated with the conclusion of the 2013 GRA; and the approval of deferral of energy supply cost variances in 2017.

Regulatory recoveries for the year ended December 31, 2017 of \$91 million were higher than recoveries of \$1 million for the same period in 2016, an increase of \$90 million. The increase for the year was primarily due to: RSP amortization and deferred fuel costs as a result of the normal operation of the RSP; reduced RSP interest due to RSP refunds during the year; adjustments related to the 2014-2015 cost deferral accounts associated with the conclusion of the 2013 GRA; and the approval of deferral of energy supply cost variances. The favourable variance was partially offset by the recognition of the 2016 cost deferral in 2016.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Other comprehensive loss

Other comprehensive loss for the three months ended December 31, 2017 was \$3 million compared to \$8 million for the same period in 2016, a decrease of \$5 million. Other comprehensive loss for the year ended December 31, 2017 was \$78 million compared to \$5 million for the same period in 2016, an increase of \$73 million. The decrease in loss for the quarter was due to favourable mark-to-market adjustments on sinking fund investments in Hydro Regulated and Nalcor, partially offset by decreases in the fair value of cash flow hedges and actuarial losses on employee future benefits. For the year, the increase in loss was primarily related to decreases in fair value of the cash flow hedges that were entered into as a result of the Muskrat Falls and LCP Transmission additional debt issue during Q2 2017 and unfavourable mark-to-market adjustments on sinking fund investments in Hydro Regulated; partially offset by in amounts recognized in profit or loss.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

CONSOLIDATED STATEMENT OF FINANCIAL POSITION HIGHLIGHTS

Significant changes in the Consolidated Statement of Financial Position between December 31, 2017 and December 31, 2016 include:

ASSETS (millions of dollars)	Increase (Decrease)	Explanation
Restricted cash	(341)	Decreased primarily as a result of capital expenditures related to Muskrat Falls and LCP Transmission; partially offset by additions related to prefunded equity requirements and investment maturities.
Short-term investments	961	Increased due to the investment of debt proceeds into structured deposit notes in Muskrat Falls and LCP Transmission.
Trade and other receivables	101	Increased due to timing of payments and higher revenue, as well as an increase in current portion of advances to a supplier in Muskrat Falls and HST receivables.
Current portion of other long-term assets	(80)	Decreased primarily due to the maturity of sinking funds associated with Hydro Regulated's Series X debentures.
Property, plant and equipment	3,137	Increased primarily due to capital expenditures related to Muskrat Falls, LCP Transmission and Hydro Regulated, as well as additions to the Maritime Link; net of depreciation, depletion and impairment related to Gull Island assets.
Intangible assets	(46)	Decreased primarily due to impairment and amortization of exploration assets, net of additions, partially offset by additions to the ongoing business systems project.
Long-term investments	298	Increased due to the investment of debt proceeds into structured deposit notes in Muskrat Falls and LCP Transmission.
Other long-term assets	(41)	Decreased primarily due to reductions in long-term advances to a supplier in relation to the construction of Muskrat Falls moving into current assets, as well as a withdrawal from Churchill Falls' reserve funds.
LIABILITIES AND EQUITY		
Short-term borrowings	(66)	Decreased primarily due to repayment of promissory notes related to Hydro Regulated.
Trade and other payables	(578)	Decreased primarily due to lower capital accruals associated with the construction of Muskrat Falls and LCP Transmission assets due to timing of payments and milestones reached during the year, partially offset by higher accrued interest related to debt issuance in Muskrat Falls and LCP Transmission.
Long-term debt including current portion	3,377	Increased primarily due to debt proceeds in Muskrat Falls, LCP Transmission and Hydro Regulated, partially offset by the maturity of Hydro Regulated's Series X debentures. See Section 5 - Liquidity and Capital Resources for additional details.
Class B limited partnership units	92	Increased due to contributions and accrued interest on the Class B partnership units.
Deferred credits, including current portion	589	Increased primarily due to deferred energy sales related to the Maritime Link.
Shareholder contributions	832	Increased due to equity injections from the Province to fund capital expenditures and prefunded equity requirements.
Reserves	(78)	Decreased primarily due to the change in the fair value of cash flow hedges in Muskrat Falls and LCP Transmission.
Regulatory deferrals, net of regulatory assets	(222)	Decreased primarily due to the disposition of cost deferrals, RSP payout to rate payers, as well as the normal operation of the RSP.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

SECTION 4: SEGMENTED RESULTS AND ANALYSIS

The following presents an overview of the Company's (loss) profit for the three and twelve months ended December 31, 2017, by business segment, in comparison to the three and twelve months ended December 31, 2016. This discussion should be read in conjunction with Note 34 of the annual audited consolidated financial statements for the year ended December 31, 2017:

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Regulated	2	23	(21)	36	19	17
Non-Regulated	(1)	(2)	1	-	(3)	3
Hydro	1	21	(20)	36	16	20
Muskrat Falls	(1)	-	(1)	(2)	(1)	(1)
Power Development	(1)	-	(1)	(2)	(1)	(1)
LCP Transmission	-	-	-	(1)	1	(2)
Churchill Falls	10	12	(2)	33	41	(8)
Other-Power Supply	(5)	1	(6)	(4)	3	(7)
Power Supply	5	13	(8)	28	45	(17)
Energy Trading	6	4	2	15	17	(2)
Commercial and Other	(51)	(1)	(50)	(52)	(1)	(51)
Energy Markets	(45)	3	(48)	(37)	16	(53)
Oil and Gas	(57)	25	(82)	9	58	(49)
Bull Arm Fabrication	8	5	3	47	20	27
Offshore Development	(49)	30	(79)	56	78	(22)
Corporate	(3)	(2)	(1)	(15)	(15)	-
Inter-Segment	(2)	(3)	1	(3)	(3)	-
(Loss) profit for the period	(94)	62	(156)	63	136	(73)

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

HYDRO

HYDRO REGULATED

The operations of Hydro Regulated are influenced by many external factors including regulation, performance of the domestic economy, weather patterns and fuel costs. The demand for electricity is met through a combination of hydroelectric generation, thermal generation and power purchases including wind generation. Hydro Regulated uses the RSP, as directed by the PUB, to annually adjust customer rates, both to smooth rate impacts for island electricity customers and to protect Hydro Regulated's profit from the majority of variations related to the HTGS fuel costs. Fuel costs fluctuate as a result of variations in electricity sales, fuel prices and hydraulic production.

The electricity rates that were in effect for customers for the first six months of the year ended December 31, 2017 reflected interim rates which were implemented on July 1, 2015. New electricity rates for customers resulting from the conclusion of Hydro Regulated's 2013 General Rate Application became effective on July 1, 2017 and have been reflected in results thereafter. Financial impacts associated with the conclusion of the 2013 GRA are reflected in Hydro Regulated's 2017 financial results.

Financial Highlights

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Revenue	151	131	20	511	515	(4)
Fuels	80	50	30	226	168	58
Power purchased	15	14	1	62	60	2
Operating costs	32	32	-	130	124	6
Depreciation and amortization	22	17	5	78	68	10
Net finance expense	15	16	(1)	65	71	(6)
Other expense	3	6	(3)	6	6	-
(Loss) profit for the period	(16)	(4)	(12)	(56)	18	(74)
Regulatory adjustments	(18)	(27)	9	(92)	(1)	(91)
Profit for the period	2	23	(21)	36	19	17

Revenue

Revenue for the three months ended December 31, 2017 was \$151 million compared to \$131 million for the same period in 2016, an increase of \$20 million. The increase for the quarter was primarily due to: the normal operation of the RSP, which reflected higher fuel prices in the second half of 2017; increased rural revenue; and increased revenue from Newfoundland Power, largely due to higher energy volumes.

Revenue for the year ended December 31, 2017 was \$511 million compared to \$515 million for the same period in 2016, a decrease of \$4 million. The decrease for the year ended was primarily due to the normal operation of the RSP, which reflected lower fuel prices for the first half of 2017 compared to the first half of 2016. This decrease was partially offset by: increased revenue from Industrial customers, largely due to higher volumes in energy and demand; and increased revenue from Newfoundland Power, largely due to increased energy volumes and demand. The impact on revenue related to the RSP and energy volumes is primarily offset in the regulatory adjustments line.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Energy supply is summarized below:

<i>For the periods ended December 31 (GWh)</i>	Three months ended			Twelve months ended		
	2017	2016	2015	2017	2016	2015
Generation:						
Hydraulic generation ¹	1,114	1,216	1,274	4,507	4,381	4,823
Hollyrood generation	594	460	466	1,671	1,621	1,459
Standby generation ^{1,2}	18	13	20	54	120	41
Thermal diesel generation	8	13	13	45	51	52
Purchases ³	417	426	429	1,683	1,613	1,666
Gross Generation	2,151	2,128	2,202	7,960	7,786	8,041
Losses	75	96	117	334	325	370
Net Generation	2,076	2,032	2,085	7,626	7,461	7,671

¹ Includes Hydro generation only.

² Includes Gas Turbine and Diesel generation.

³ Purchases include generation from Exploits, recall energy for use in Labrador, wind and other sources.

Energy sales are summarized below:

<i>For the periods ended December 31 (GWh)</i>	Three months ended			Twelve months ended		
	2017	2016	2015	2017	2016	2015
Newfoundland Power	1,600	1,583	1,667	5,896	5,845	6,072
Hydro Rural	315	316	283	1,142	1,105	1,100
Industrials	161	133	135	588	511	499
	2,076	2,032	2,085	7,626	7,461	7,671

The average base rate revenue for Hydro Regulated island interconnected customers¹ is summarized below:

<i>For the year ended December 31</i>	2017	2016	2015
Wholesale Utility:			
First Block Energy (¢/KWh)	2.866	3.506	3.506
Second Block Energy (¢/KWh)	9.823	9.509	9.060
Demand (\$/KW)	4.54	4.32	4.16
Island Industrial:			
Energy (¢/KWh)	4.017	4.069	3.866
Demand (\$/KW)	8.18	8.38	7.03

¹ Excludes rural island and Labrador interconnected customers, secondary energy, specifically assigned charges and the impact of the RSP.

The above table illustrates the average base rate revenue per kWh and kW generated from Island Interconnected customers for the years ended December 31, 2017, 2016 and 2015. Base rate revenue excludes the impact of changes in customer rates as a result of activity in the RSP as well as any regulatory adjustments not reflected in the revenue line. Although activity in the RSP impacts the revenue line, it is largely offset in the regulatory adjustments line.

Fuels

Fuel costs for the three months ended December 31, 2017 were \$80 million compared to \$50 million for the same period in 2016, an increase of \$30 million. The increase for the quarter was primarily due to an increase in both No. 6 fuel price and volume.

Fuel costs for the year ended December 31, 2017 were \$226 million compared to \$168 million for the same period in 2016, an increase of \$58 million. The increase for the year was primarily due to increases in No. 6 fuel and gas turbine fuel prices. This increase was partially offset by a decrease in gas turbine fuel volume.

The majority of variances in fuel are either offset through the RSP or through other regulatory mechanisms in the regulatory adjustments line.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

The following tables summarize fuel consumed and average price:

<i>For the periods ended December 31</i>	Three months ended			Twelve months ended		
	2017	2016	2015	2017	2016	2015
No. 6 fuel consumption: Millions of barrels	1.0	0.8	0.8	2.8	2.7	2.4
Average price (CAD/bbl)	\$71.85	\$55.08	\$60.39	\$68.60	\$46.40	\$67.21
Gas Turbine fuel consumption: Millions of liters	9.1	6.2	8.0	28.3	50.1	20.5
Average price (CAD/liter)	\$0.72	\$0.64	\$0.66	\$0.69	\$0.58	\$0.75
Diesel fuel consumption: Millions of liters	3.8	4.2	4.3	15.3	16.1	16.1
Average price (CAD/liter)	\$0.96	\$0.92	\$0.96	\$0.94	\$0.89	\$1.01

Fuel costs are summarized below:

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	2015	2017	2016	2015
No. 6 fuel and other	70	43	45	192	125	161
Gas Turbine Fuel	7	4	5	20	29	15
Diesel	3	3	5	14	14	17
	80	50	55	226	168	193

Power purchased

Power purchased for the three months and year ended December 31, 2017 was comparable with the same periods in 2016.

Operating costs

Operating costs for the three months ended December 31, 2017 were comparable with the same period in 2016. Operating costs for the year ended December 31, 2017 were \$130 million compared to \$124 million for the same period in 2016, an increase of \$6 million. The increase for the year ended was primarily due to higher costs associated with salaries and benefits, insurance, and maintenance and materials. These increases were partially offset by a reduction in equipment rental expense.

Depreciation and amortization

Depreciation and amortization for the three months ended December 31, 2017 was \$22 million compared to \$17 million for the same period in 2016, an increase of \$5 million. Depreciation and amortization for the year ended December 31, 2017 was \$78 million compared to \$68 million for the same period in 2016, an increase of \$10 million. The increase for the three months and year ended December 31, 2017 was due to increased levels of investment in property, plant and equipment.

Net finance expense

Net finance expense for the three months ended December 31, 2017 was comparable with the same period in 2016. Net finance expense for the year ended December 31, 2017 was \$65 million compared to \$71 million for the same period in 2016, a decrease of \$6 million. The decrease for the year ended was primarily due to higher capitalized interest related to an increase in Hydro Regulated's capital program and reduced interest resulting from the retirement of Hydro Regulated's long-term debt in 2016 that was refinanced during 2017 at lower interest rates. These decreases were partially offset by higher short-term borrowing levels and lower income associated with sinking funds as a result of the repayment of Series X debentures.

Other expense

Other expense for the three months ended December 31, 2017 was \$3 million compared to \$6 million for the same period in 2016, a decrease of \$3 million. Other expense for the year ended December 31, 2017 was comparable with the same period in 2016. The decrease in expense for the quarter was primarily related to lower losses on disposal of assets.

Regulatory adjustments

Regulatory recoveries for the three months ended December 31, 2017 of \$18 million were lower than recoveries of \$27 million for the same period in 2016, a decrease of \$9 million. The variance in the quarter was primarily due to the approval of the 2016 cost deferral in Q4 2016 and RSP amortization. This was partially offset by: RSP deferred fuel costs as a result of the normal operation of the RSP;

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

reduced RSP interest due to lower RSP balances; adjustments for amounts related to the 2014-2015 cost deferral accounts recognized in Q4 2016 associated with the conclusion of the 2013 GRA; and the approval of deferral of energy supply cost variances in 2017.

Regulatory recoveries for the year ended December 31, 2017 of \$92 million were higher than recoveries of \$1 million for the same period in 2016, an increase of \$91 million. The increase for the year was primarily due to: RSP amortization and deferred fuel costs as a result of the normal operation of the RSP; reduced RSP interest due to RSP refunds during the year; adjustments related to the 2014-2015 cost deferral accounts associated with the conclusion of the 2013 GRA; and the approval of deferral of energy supply cost variances. The favourable variance was partially offset by the recognition of the 2016 cost deferral in 2016.

HYDRO NON-REGULATED

Hydro Non-Regulated activities include the sale of power, purchased from Churchill Falls, to mining operations in Labrador West as well as costs related to operations that Hydro manages that are not subject to rate regulation by the PUB.

Financial Highlights

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Revenue	10	11	(1)	40	40	-
Power purchased	10	10	-	39	39	-
Operating costs	1	3	(2)	1	4	(3)
Loss for the period	(1)	(2)	1	-	(3)	3

Revenue

Revenue for the three months and year ended December 31, 2017 was comparable with the same periods in 2016.

Power Purchased

Power purchased for the three months and year ended December 31, 2017 was comparable with the same periods in 2016.

Operating costs

Operating costs for the three months ended December 31, 2017 were comparable to the same period in 2016. Operating costs for the year ended December 31, 2017 were \$1 million compared to \$4 million for the same period in December 31, 2016, a decrease of \$3 million. The decrease for the year was primarily due to bad debt expense recognized in Q4 2016.

POWER DEVELOPMENT

MUSKRAT FALLS

Muskrat Falls includes the development activities of the 824 MW hydroelectric generating facility currently under construction in Labrador on the Lower Churchill River. Once construction is complete this asset and its operation will become part of the Power Supply segment.

Financial Highlights

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Operating costs	1	-	1	1	-	1
Other expense	-	-	-	1	1	-
Loss for the period	(1)	-	(1)	(2)	(1)	(1)

Results of Muskrat Falls for the three months and year ended December 31, 2017 were comparable with the same periods in 2016. See Section 5 – Liquidity and Capital Resources for additional details on capital expenditures incurred in the segment during the periods ended December 31, 2017.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

POWER SUPPLY

LCP TRANSMISSION

LCP Transmission includes the construction and operation of the LIL and LTA, which consist of transmission lines connecting the Muskrat Falls hydroelectric facility, the Churchill Falls hydroelectric facility, and certain portions of the transmission system in Labrador to the island of Newfoundland.

Financial Highlights

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Operating costs	1	1	-	3	2	1
Net finance income	(1)	(1)	-	(2)	(2)	-
Other income	-	-	-	-	(1)	1
(Loss) profit for the period	-	-	-	(1)	1	(2)

Results of LCP Transmission for the three months and year ended December 31, 2017 were comparable with the same periods in 2016. See Section 5 – Liquidity and Capital Resources for additional details on capital expenditures incurred in the segment during the periods ended December 31, 2017.

CHURCHILL FALLS

Churchill Falls is the owner and operator of the Churchill Falls Generating Station, with a rated capacity of 5,428 MW. The 1969 Power Contract, and a Renewal Contract that commenced September 1, 2016 and expiring August 31, 2041, provide for the sale of electricity from this facility to Hydro-Québec. In addition, two power purchase agreements effective March 9, 1998 and January 1, 2015, provide for the sale of electricity to Hydro for use domestically and for resale in export markets.

Financial Highlights

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Revenue	27	27	-	92	97	(5)
Operating costs	12	11	1	44	44	-
Depreciation and amortization	5	5	-	18	17	1
Net finance income	-	-	-	(1)	(1)	-
Preferred dividends	-	(1)	1	(2)	(4)	2
Profit for the period	10	12	(2)	33	41	(8)

Revenue

Revenue for the three months ended December 31, 2017 was comparable with the same period in 2016. Revenue for the year ended December 31, 2017 was \$92 million compared to \$97 million for the same period in 2016, a decrease of \$5 million. The decrease was primarily due to lower energy sales to Hydro-Québec and Hydro, as a result of a 20% decrease in the rate charged in accordance with the Renewal Contract which came into effect September 1, 2016. The decrease is partially offset by an increase in GWh billed to Hydro-Québec combined with higher revenue achieved under the Guaranteed Winter Availability Contract (GWAC) between Churchill Falls and Hydro-Québec.

For the three months ended December 31, 2017, Churchill Falls derived 36% of its revenue from sales to Hydro-Québec under the Power Contract and Renewal Contract (2016 – 35%), 36% from the GWAC (2016 – 37%) and 28% from other revenue (2016 – 28%). Other revenue includes the sale of energy to Hydro.

For the year ended December 31, 2017, Churchill Falls derived 42% of its revenue from sales to Hydro-Québec under the Power Contract and Renewal Contract (2016 – 44%), 26% from the GWAC (2016 – 25%) and 32% from other revenue (2016 – 31%). Other revenue includes the sale of energy to Hydro.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Operating Costs

Operating costs for the three months and year ended December 31, 2017 were comparable with the same periods in 2016.

Depreciation and amortization

Depreciation and amortization for the three months and year ended December 31, 2017 were comparable with the same periods in 2016.

Net finance income

Net finance income for the three months and year ended December 31, 2017 were comparable with the same periods in 2016.

Preferred dividends

Preferred dividends for the three months and year ended December 31, 2017, were comparable to the same periods in 2016.

OTHER – POWER SUPPLY

Other-Power Supply includes revenues and costs recovered from Hydro-Québec associated with Nalcor's operation of the Menihék Generating Station, the Maritime Link (which is owned by Emera, but consolidated by Nalcor), administration and community development costs related to Power Supply, and costs associated with the management of LCP construction.

Financial Highlights

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Revenue	3	1	2	9	6	3
Operating costs	8	-	8	13	3	10
(Loss) profit for the period	(5)	1	(6)	(4)	3	(7)

Revenue

Revenue for the three months ended December 31, 2017 was comparable to the same period in 2016. Revenue for the year ended December 31, 2017 was \$9 million compared to \$6 million for the same period in 2016, an increase of \$3 million. The increase was primarily associated with the Menihék Generating Station and is due to higher revenue associated with capital projects and operating expenses billed to Hydro-Québec.

Operating Costs

Operating costs for the three months ended December 31, 2017 were \$8 million compared to \$nil for the same period in 2016, an increase of \$8 million. Operating costs for the year ended December 31, 2017 were \$13 million compared to \$3 million for the same period in 2016, an increase of \$10 million. The increase for the periods was primarily due to costs incurred as part of the CDA, as well as costs associated with the Menihék Generating Station due to higher operating costs related to work performed for Hydro-Québec.

ENERGY MARKETS

ENERGY TRADING

The revenue and profit in this segment is derived primarily from the sale of available Recapture, the block of 300MW of firm energy and capacity pursuant to the Power Contract which Churchill Falls has agreed to sell and deliver to Hydro. The Recapture is sold to markets and customers in eastern Canada and the northeastern United States.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Financial Highlights

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Revenue	14	10	4	48	43	5
Power purchased	1	1	-	4	4	-
Operating costs	2	1	1	5	5	-
Transmission rental and market fees	6	5	1	25	22	3
Other income	(1)	(1)	-	(1)	(5)	4
Profit for the period	6	4	2	15	17	(2)

Revenue

Revenue for the three months ended December 31, 2017 was \$14 million compared to \$10 million in 2016, an increase of \$4 million. Revenue for the year ended 2017 was \$48 million compared to \$43 million in 2016, an increase of \$5 million. The increase in revenue was primarily due to higher average export electricity prices in the winter months of 2017.

Prices and volumes for the three months and year ended December 31, 2017 with 2016 and 2015 comparatives for sales in export markets are summarized in the table below.

<i>For the periods ended December 31</i>	Three months ended			Twelve months ended		
	2017	2016	2015	2017	2016	2015
Average Export Electricity Price (USD/MWh) ¹	28	21	19	23	20	25
Realized Export Electricity Price (USD/MWh) ²	29	21	26	23	22	31
Realized Export Electricity Price (CAD/MWh) ³	37	28	29	31	29	36
Export sales (GWh)	359	378	373	1,594	1,627	1,569

¹The Average Export Electricity Price reflects prices realized in the export market.

²The Realized Export Price (USD) includes the impact of electricity commodity price hedges and financial transmission rights.

³The Realized Export Electricity Price (CAD) includes the impact of electricity commodity price hedges, financial transmission rights and foreign exchange.

Power purchased

Power purchased for the three months and year ended December 31, 2017 was comparable to the same periods in 2016.

Operating costs

Operating costs for the three months and year ended December 31, 2017 were comparable to the same periods in 2016.

Transmission rental and market fees

Transmission rental and market fees for the three months ended December 31, 2017 were comparable to the same period in 2016. Transmission rental and market fees for the year ended 2017 were \$25 million compared to \$22 million in 2016, an increase of \$3 million due to an increase in transmission purchased to deliver energy to export markets and an increase in firm transmission rates compared to 2016.

Other income

Other income for the three months ended December 31, 2017 was comparable to 2016. Other income for the year ended 2017 was \$1 million compared to \$5 million in 2016, a decrease of \$4 million. The decrease is primarily due to Energy Trading not holding any commodity contracts in 2017, while there were favorable settlements on commodity contracts held during the first six months of 2016, as well as unfavourable foreign exchange on USD transactions.

COMMERCIAL AND OTHER

Commercial and other includes costs associated with business development activities related to exploring additional markets and sources for future energy generation and transmission. Included in Commercial and Other are assets of \$140 million, representing historical costs incurred from 1998 to 2017 related to pre-development activities for the Gull Island power development. These costs primarily relate to environmental assessments, impact and benefits agreement, engineering, commercial, and related activities.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Financial Highlights

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Operating costs	-	-	-	1	-	1
Depreciation, amortization and impairment	51	1	50	51	1	50
Loss for the period	(51)	(1)	(50)	(52)	(1)	(51)

Non-GAAP Operating Loss Disclosure

Reconciliation of Commercial and Other loss to operating loss for the three months and year ended December 31, 2017 is as follows:

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Loss for the period	(51)	(1)	(50)	(52)	(1)	(51)
Impairment of property, plant and equipment	51	-	51	51	-	51
Operating loss for the period	-	(1)	1	(1)	(1)	-

Operating costs

Operating costs for the three months and year ended December 31, 2017 were comparable to the same periods in 2016.

Depreciation, amortization and impairment

Depreciation, amortization and impairment for the three months and year ended December 31, 2017 was \$51 million compared to \$1 million for the same period in 2016, an increase of \$50 million. The increase is related to an impairment of older Gull Island costs, previously capitalized, which Management has assessed as no longer having future economic benefit towards the project. The impairment assessment included reviewing older costs that no longer contribute to the future economic value of the project due to the passage of time. The majority of costs included as part of the impairment were incurred prior to 2005 and related to commercial, financing and other related activities. Nalcor continues to carry capitalized costs of \$140 million related to Gull Island which management believes have future value towards the project.

See Section 5 – Liquidity and Capital Resources for additional details on capital expenditures incurred in the segment during the periods ended December 31, 2017.

OFFSHORE DEVELOPMENT

OIL AND GAS

Nalcor Oil and Gas is currently a joint venture working interest partner in three developments in the Newfoundland and Labrador offshore. It owns a 4.9% working interest in the Hebron oil field, the Province's fourth offshore oil project, which produced first oil in November 2017; a 5.0% working interest in the WR Extension, which produced first oil from the North Amethyst field in May 2010; and a 10.0% working interest in the HSE, which produced first oil in June 2011.

Financial Highlights

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Revenue	65	52	13	224	140	84
Operating costs	3	2	1	8	8	-
Production, marketing and transportation costs	13	8	5	36	26	10
Depreciation, depletion, amortization and impairment	100	15	85	152	48	104
Exploration and evaluation	-	2	(2)	1	2	(1)
Net finance expense	1	-	1	3	3	-
Other expense (income)	5	-	5	15	(5)	20
(Loss) profit for the period	(57)	25	(82)	9	58	(49)

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Non-GAAP Operating Profit Disclosure

Reconciliation of Oil and Gas' (loss) profit to operating profit for the three months and year ended December 31, 2017 is as follows:

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
(Loss) profit for the period	(57)	25	(82)	9	58	(49)
Impairment of exploration intangible asset	81	-	81	81	-	81
Operating profit for the period	24	25	(1)	90	58	32

Revenue

Revenue for the three months ended December 31, 2017 was \$65 million compared to \$52 million for the same period in 2016, an increase of \$13 million. Revenue for the year ended December 31, 2017 was \$224 million compared to \$140 million for the same period in 2016, an increase of \$84 million. The increase for the quarter and year was primarily due to higher average Dated Brent prices per barrel as compared to the same periods in 2016, along with an increase in production volumes.

Oil price data and production for the three months and year ended December 31, 2017 with 2016 and 2015 comparatives are summarized in the table below.

<i>For the periods ended December 31</i>	Three months ended			Twelve months ended		
	2017	2016	2015	2017	2016	2015
Average Dated Brent Price (USD/bbl) ¹	64	51	39	54	46	48
Realized Price (USD/bbl) ²	62	51	54	54	48	65
Realized Price (CAD/bbl) ³	80	69	71	70	64	83
Oil Production (Mbbbls)	809	733	225	3,235	2,226	525

¹The Average Dated Brent Price reflects prices available in the market adjusted for any premium or discount.

²The Realized Price (USD) includes the impact of oil commodity price hedges.

³The Realized Price (CAD) includes the impact of oil commodity price hedges and foreign exchange.

Operating costs

Operating costs for the three months and year ended December 31, 2017 were comparable with the same periods in 2016.

Production, marketing and transportation costs

Production, marketing and transportation costs for the three months ended December 31, 2017 were \$13 million compared to \$8 million for the same period in 2016, an increase of \$5 million. Production, marketing and transportation costs for the year ended December 31, 2017 were \$36 million compared to \$26 million for the same period in 2016, an increase of \$10 million. The increase for the quarter and year was primarily due to an increase in production volumes and increased project operating costs associated with the joint venture projects.

Depreciation, depletion, amortization and impairment

Depreciation, depletion, amortization and impairment costs for the three months ended December 31, 2017 were \$100 million compared to \$15 million for the same period in 2016, an increase of \$85 million. Depreciation, depletion, amortization and impairment costs for the year ended December 31, 2017 were \$152 million compared to \$48 million for the same period in 2016, an increase of \$104 million. The increase for the quarter was primarily due to an \$81 million impairment of exploration intangible assets as well as an increase in depletion associated with Hebron and WR production. The annual increase was primarily due to impairment of exploration intangible assets and an increase in depletion associated with higher production volumes for the three joint venture projects.

The exploration program has been successful in making data available, attracting new participants to the NL offshore, supporting increased land sales, and identification of previously unknown prospects. This work has generally provided benefits to the Province and the future development of the oil and gas industry. However, because of the time horizon required to bring a project to the development stage, the period for Nalcor to realize a return on its investment is some considerable number of years away. Nalcor had previously been amortizing each exploration program over a six year period. In 2017 Nalcor made the decision to write down the balance of the unamortized exploration costs. The resulting impact was reducing 2017 profit, but will result in no amortization in future years.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Exploration and evaluation

Exploration and evaluation expense for the three months and year ended December 31, 2017 was consistent with the same period in 2016.

Net finance expense

Net finance expense for the three months and year ended December 31, 2017 was consistent with the same period in 2016.

Other expense (income)

Other expense for the three months ended December 31, 2017 was \$5 million compared to \$nil for the same period in 2016, an increase of \$5 million. Other expense for the year ended December 31, 2017 was \$15 million compared to other income of \$5 million for the same period in 2016, an increase in expense of \$20 million. The increases for both the quarter and the year were primarily related to losses associated with the disposal of assets due to the conclusion of Hebron construction; unfavourable foreign exchange on USD transactions; and net losses on the settlement of oil commodity contracts, as compared to net gains on settlement for the same periods in 2016.

RESERVES

Oil and Gas contracts independent reserve evaluators to prepare reports on remaining oil reserves related to its working interest in offshore developments. Gross reserves represent Oil and Gas' working interest in remaining reserves, while net reserves represent remaining reserves less royalties. Remaining reserve data for both proved and probable reserves to be recovered as at December 31, 2017 with 2016 comparatives are summarized in the table below:

<i>As at December 31 (Mbbbls)</i>	2017		2016	
	Light and Medium Oil Gross	Net	Light and Medium Oil Gross	Net
Developed	12,294	8,659	11,385	8,271
Undeveloped	10,545	10,365	11,120	10,243
Total Proved	22,839	19,024	22,505	18,514
Probable	39,823	32,101	41,034	32,986
Total Proved Plus Probable	62,662	51,125	63,539	51,500

BULL ARM FABRICATION

Revenue related to Bull Arm Fabrication is primarily generated through leasing arrangements. The site was under sublease to EMCP until December 31, 2017 for completion of the Hebron Project. During Q2 2017, Bull Arm Fabrication finalized the close-out value of the EMCP multi-year sublease agreement and recorded a one-time adjustment to lease revenue of approximately \$26 million.

Financial Highlights

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Revenue	7	5	2	48	21	27
Operating costs	-	-	-	1	1	-
Other income	(1)	-	(1)	-	-	-
Profit for the period	8	5	3	47	20	27

Non-GAAP Operating Profit Disclosure

Reconciliation of Bull Arm Fabrications' profit to operating profit for the three months and year ended December 31, 2017 is as follows:

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Profit for the period	8	5	3	47	20	27
Close-out of Hebron sublease agreement	-	-	-	(26)	-	(26)
Operating profit for the period	8	5	3	21	20	1

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Revenue

Revenue for the three months ended December 31, 2017 was comparable to the same period in 2016. Revenue for the year ended December 31, 2017 was \$48 million compared to \$21 million for the same period in 2016, an increase of \$27 million. The increase for the year was primarily due to the recognition of a one-time adjustment to lease revenue related to the close-out value of the EMCP sublease agreement.

Operating costs

Operating costs for the three months and year ended December 31, 2017 were comparable with the same periods in 2016.

Other income

Other income for the three months and year ended December 31, 2017 was comparable with the same periods in 2016.

CORPORATE

Financial Highlights

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Operating costs	2	-	2	12	13	(1)
Depreciation and amortization	1	1	-	1	1	-
Net finance expense	-	1	(1)	1	1	-
Other expense	-	-	-	1	-	1
Loss for the period	(3)	(2)	(1)	(15)	(15)	-

Results of Corporate for the three months and year ended December 31, 2017 were comparable with the same periods in 2016.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

SECTION 5: LIQUIDITY AND CAPITAL RESOURCES

CASH FLOW HIGHLIGHTS

<i>For the year ended December 31 (millions of dollars)</i>	2017	2016	Variance
Cash and cash equivalents, beginning of year	143	149	(6)
Net cash provided from operating activities	210	219	(9)
Net cash used in investing activities	(4,537)	(1,623)	(2,914)
Net cash provided from financing activities	4,327	1,398	2,929
Cash and cash equivalents, end of year	143	143	-

Operating activities:

<i>For the year ended December 31 (millions of dollars)</i>	2017	2016	Variance
Net cash provided from operating activities	210	219	(9)

Cash provided from operating activities for the year ended December 31, 2017 was \$210 million compared to \$219 million for the same period in 2016. The decrease in cash resources of \$9 million was primarily due to unfavourable operating working capital variances partially offset by increased cash provided from profit for the year.

Investing Activities:

<i>For the year ended December 31 (millions of dollars)</i>	2017	2016	Variance
Additions to property, plant and equipment and intangible assets	(2,799)	(2,777)	(22)
Change in long-term receivables	28	(24)	52
Change in investments (including short-term)	(1,259)	992	(2,251)
Changes in non-cash working capital balances	(623)	177	(800)
Change in sinking funds	90	(6)	96
Other	26	15	11
Net cash used in investing activities	(4,537)	(1,623)	(2,914)

Cash used in investing activities during the year ended December 31, 2017 was \$4,537 million compared to \$1,623 million for the same period in 2016. The increase in cash used in investing activities of \$2,914 million was primarily due to increased investment in structured deposit notes by Muskrat Falls and LCP Transmission, using proceeds from the debt issued in Q2 2017. Changes in non-cash working capital balances, specifically decreases in capital accruals, maturities of sinking funds related to Hydro Regulated's Series X debentures and increased additions to property, plant and equipment and intangible assets.

Financing Activities:

<i>For the year ended December 31 (millions of dollars)</i>	2017	2016	Variance
Proceeds from long-term debt	3,516	-	3,516
Retirement of long-term debt	(150)	(225)	75
Change in restricted cash	341	458	(117)
Class B limited partnership unit contributions	55	168	(113)
Change in short-term borrowings	(66)	338	(404)
Change in shareholder contributions	832	657	175
Rate Stabilization Plan payout	(131)	-	(131)
Settlement of cash flow hedges	(67)	-	(67)
Other	(3)	2	(5)
Net cash provided from financing activities	4,327	1,398	2,929

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

During 2017, \$4,327 million was provided from financing activities, compared to \$1,398 million in 2016. The increase of \$2,929 million was primarily due to proceeds of \$2.9 billion of additional debt in Muskrat Falls and LCP Transmission, as well as Hydro Regulated's issuance of \$300 million in Series AF debentures in January 2017, which replaced the retirement of Series AE that matured in Q4 2016, \$300 million in Series 1A debt issued on December 31, 2017, and increased shareholder contributions. These increases were partially offset by lower promissory notes at the end of 2017, the RSP payout that has been refunded to rate payers to date and cash required for the settlement of cash flow hedges in Muskrat Falls and LCP Transmission.

CAPITAL RESOURCES

Nalcor's capital resources consist primarily of cash and cash equivalents, restricted cash, short-term investments, long-term investments and equity from the Province. These capital resources are used to fund the Company's consolidated capital resource requirements, which continue to include working capital needs, capital expenditures, development costs, and the servicing and repayment of debt. Capital resources are managed at the subsidiary level, taking into account the specific cash flow and liquidity needs of each subsidiary. Cash from operations is a primary source of funding for most subsidiaries. Cash from operations depends on a number of factors including commodity prices, regulatory decisions from the PUB relating to electricity rates and the associated timing and recovery of those rates, foreign exchange rates, oil production and electricity export volume. As a result, Nalcor monitors cash from operations for each subsidiary and where necessary, additional sources of liquidity are put in place. In some cases, subsidiaries have access to long-term debt financing and equity from the Province.

HYDRO REGULATED

Capital resource requirements for Hydro Regulated consist primarily of working capital needs, capital expenditures and debt servicing and repayment. Hydro Regulated's capital resources consist primarily of cash from operations, cash and cash equivalents, sinking funds and access to a \$300 million government guaranteed promissory note program. As at December 31, 2017, there were \$144 million in notes outstanding under this program (2016 - \$210 million). Hydro Regulated has access to an additional \$200 million committed bank credit facility. As at December 31, 2017, there were no amounts drawn on the facility (2016 - \$nil). Previously, Hydro Regulated had maintained a \$50 million demand operating facility with the same bank. In July 2017, Hydro Regulated converted its \$50 million unsecured demand operating facility with its banker to a \$200 million committed revolving term credit facility, with a maturity date of July 27, 2019.

Historically, Hydro Regulated addressed longer-term capital funding requirements by issuing government guaranteed long-term debt in the domestic capital markets. However, in December 2017, Hydro Regulated's process changed to one whereby the Province issues debt specifically on Hydro Regulated's behalf and lends the proceeds to Hydro Regulated on a cost recovery basis. The Province authorized funding up to \$700 million, which includes \$225 million to repay an outstanding promissory note to the Province through Nalcor, due March 31, 2018. As at December 31, 2017, \$300 of the \$700 million authorized has been issued.

Management believes that existing capital resources, inclusive of the new arrangement with the Province, will be sufficient to fund planned capital expenditures, debt servicing requirements and working capital needs for 2018 and beyond. However, access to long-term debt through the Province remains an important consideration for funding Hydro Regulated's capital resource requirements.

CHURCHILL FALLS

Capital resource requirements consist primarily of working capital needs, reserve fund payments and capital expenditures. Churchill Falls capital resources consist primarily of cash from operations, cash and cash equivalents, short-term investments and long-term investments. In addition, Churchill Falls has access to a \$10 million unsecured demand operating credit facility. There were no amounts drawn on this facility as at December 31, 2017 (2016 - \$nil), however, \$1.0 million of the borrowing limit has been used to issue two irrevocable letters of credit (2016 - \$1.0 million). Churchill Falls also has access to a reserve fund, which when fully funded totals \$75 million, and can be used to fund capital expenditures relating to Churchill Falls' existing facilities and their replacement, subject to the terms and conditions established in the Shareholder's Agreement. In December 2017, the remaining reserves were withdrawn to fund a portion of capital expenditures. Contributions will be made over the next five years to replace all funds withdrawn.

As at December 31, 2017, short-term investments and long-term investments consisted of a series of fully redeemable Guaranteed Investment Certificates, which Management purchased to increase the return on excess cash held by Churchill Falls. Because these instruments are fully redeemable, these balances are readily convertible to cash if needed to fund capital resource requirements.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Management believes existing capital resources will be sufficient to fund planned 2018 capital expenditures, reserve fund repayments and to meet current and future working capital needs.

OIL AND GAS

Capital resource requirements consist primarily of working capital needs and capital expenditures. Oil and Gas' capital resources consist primarily of cash from operations and access to a \$30.0 million unsecured demand operating credit facility. While there were no amounts drawn on this facility at December 31, 2017 (2016 - \$nil), \$5.4 million of the borrowing limit has been used to issue two irrevocable letters of credit (2016 - \$0.5 million). Management believes these existing capital resources will be sufficient to fund planned 2018 capital expenditures for Oil and Gas while meeting current and future working capital needs.

ENERGY TRADING AND BULL ARM FABRICATION

Capital resource requirements for Energy Trading and Bull Arm Fabrication are primarily limited to working capital needs. For Energy Trading and Bull Arm Fabrication, capital resources consist primarily of cash from operations and, in the case of Energy Trading, access to a \$20.0 million demand operating credit facility. As at December 31, 2017, Energy Trading had no amounts drawn on this facility (2016 - \$nil). Management believes these existing capital resources will be sufficient to meet current and future working capital needs for Energy Trading and Bull Arm Fabrication.

MUSKRAT FALLS AND LCP TRANSMISSION

Capital resource requirements for Muskrat Falls and LCP Transmission consist primarily of capital expenditures in connection with construction of the Lower Churchill Project. The primary source of financing for Muskrat Falls and LCP Transmission will continue to be the credit facilities and equity contributions from the Province. Subsequent to the long-term debt issue in Muskrat Falls and LCP Transmission in May 2017, new working capital facilities were established in the amount of \$75 million as previous working capital facilities related to Muskrat Falls and LTA had been drawn down fully during the first quarter of 2017. Management believes these capital resources will be sufficient to fund 2018 planned capital expenditures.

ADDITIONAL LIQUIDITY

Nalcor maintains a \$250 million CAD or USD equivalent committed revolving term credit facility with its bank which serves as an additional source of liquidity available to each of the subsidiaries. There were no amounts drawn on this facility as at December 31, 2017 (2016 - \$nil), however \$34 million of the borrowing limit has been used to issue 15 irrevocable letters of credit (2016 - \$34 million was used to issue 14 letters of credit). Two letters of credit, totaling \$25 million, are on behalf of Oil and Gas to ensure compliance with regulations relating to petroleum and natural gas exploration and production activities. Another 12 letters, totaling \$8 million are on behalf of Energy Trading and relate to power purchase and sale contracts with various independent system operators, transmission providers and bilateral counterparties. An additional letter in the amount of \$1 million was issued by Nalcor in support of a bid for the supply of energy.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

As at December 31, 2017 and December 31, 2016, external credit facilities are as follows:

	December 31, 2017			Available
<i>As at (millions of dollars)</i>	Limit	Drawn	Letters of Credit Issued	Limit
Revolving Term Facilities:				
Nalcor Energy	250	-	34	216
Hydro Regulated	200	-	-	200
Demand Operating Facilities:				
Oil and Gas	30	-	5	25
Churchill Falls	10	-	1	9
Energy Trading	20	-	-	20
Muskrat Falls	61	-	-	61
LCP Transmission	89	-	-	89
Promissory Notes:				
Hydro Regulated	300	144	-	156
Total credit facilities	960	144	40	776

	December 31, 2016			Available
<i>As at (millions of dollars)</i>	Limit	Drawn	Letters of Credit Issued	Limit
Revolving Term Facilities:				
Nalcor	250	-	34	216
Demand Operating Facilities:				
Hydro Regulated	50	-	-	50
Oil and Gas	30	-	1	29
Churchill Falls	10	-	1	9
Energy Trading	20	-	-	20
Muskrat Falls	49	-	-	49
LCP Transmission	42	-	-	42
Promissory Notes:				
Hydro Regulated	300	210	-	90
Total credit facilities	751	210	36	505

Promissory Notes

Hydro Regulated utilized its government guaranteed promissory note program to fulfill its short-term funding requirements. As at December 31, 2017, there were \$144 million in promissory notes outstanding with a maturity date of January 3, 2018 bearing an interest rate of 1.13% (2016 - \$210 million bearing an interest rate of 0.63%). Upon maturity, the promissory notes were reissued with a maturity date of January 16, 2018 and bearing an interest rate of 1.17%. On January 16, 2018, the promissory notes were once again reissued.

Other Promissory Notes

On October 12, 2016, Nalcor issued a \$225 million promissory note to the Province with a maturity date of January 11, 2017 at a rate of 0.90%. Nalcor lent the proceeds to Hydro in exchange for a promissory note with identical terms and conditions. Hydro Regulated used the proceeds to retire long-term debentures. The original promissory note was refinanced three additional times during 2017. The most recent refinancing occurred on September 29, 2017, with the outstanding promissory note bearing interest at a rate of 1.845% and maturing on March 30, 2018. Hydro Regulated intends to repay the note to Nalcor using proceeds from new long-term funding prior to March 30, 2018, if market conditions are favourable.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

LONG-TERM DEBT

In addition to credit facilities, Nalcor utilizes long-term debt and/or equity contributions from the Province to fund capital resource requirements when necessary. The use of long-term debt to fund capital resource requirements is limited to cases where there is reasonable certainty that operating cash flows will be sufficient to service the debt while maintaining an appropriate level of stand-alone creditworthiness.

CAPITAL STRUCTURE

Nalcor's consolidated capital structure and associated performance indicators are shown in the table below:

<i>As at (millions of dollars)</i>	December 31 2017	December 31 2016
Short-term borrowings	369	435
Current portion of long-term debt	7	143
Long-term debt (net of sinking funds)	9,196	5,606
Class B limited partnership units	491	399
Total debt	10,063	6,583
Total shareholder's equity	5,081	4,264
Debt to capital ¹	66%	61%
Fixed rate debt as a percentage of total indebtedness ¹	91%	87%

¹The above noted ratios are Non-GAAP financial measures. Please refer to Section 8: Non-GAAP Financial Measures.

On January 20, 2017, Hydro Regulated issued new long-term debt of \$300 million of Series AF debentures. The debentures mature on December 31, 2045 with a coupon rate of 3.6%, paid semi-annually.

In May 2017, Muskrat Falls and LCP Transmission borrowed new long-term debt in the amount of \$2.9 billion, by way of a series of 138 bonds with maturities every six months beginning in December 2020 and maturing in June 2057. Coupon rates range from 1.14% to 2.86%.

On July 14, 2017, Hydro Regulated repaid its Series X debentures of \$150 million.

On December 20, 2017, Hydro Regulated issued new long-term debt of \$300 million, Series 1A. The Province issued debt specifically on Hydro Regulated's behalf and lent the proceeds to Hydro Regulated. The debt matures on October 17, 2048 with a coupon rate of 3.70%, paid semi-annually.

On March 8, 2018, the Province issued long-term debt with a face value of \$300.0 million, specifically on Hydro's behalf. The debt matures on October 17, 2048 with a coupon rate of 3.70% paid semi-annually. Nalcor expects to use a portion of the proceeds to repay the \$225.0 million promissory note to the Province.

During the year ended December 31, 2017, Emera NL contributed \$55 million in Class B Limited Partnership Units and an additional \$37 million of accrued interest was recognized.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

CAPITAL EXPENDITURES

<i>For the periods ended December 31 (millions of dollars)</i>	Three months ended			Twelve months ended		
	2017	2016	Variance	2017	2016	Variance
Regulated	107	96	11	344	221	123
Non-Regulated	-	1	(1)	-	1	(1)
Hydro	107	97	10	344	222	122
Muskrat Falls ¹	316	222	94	1,137	976	161
Power Development	316	222	94	1,137	976	161
LCP Transmission ¹	216	369	(153)	1,140	1,315	(175)
Churchill Falls	11	6	5	46	41	5
Other	155	94	61	593	491	102
Power Supply	382	469	(87)	1,779	1,847	(68)
Energy Trading	-	-	-	-	-	-
Commercial and Other	1	-	1	1	1	-
Energy Markets	1	-	1	1	1	-
Oil and Gas	21	63	(42)	161	236	(75)
Bull Arm Fabrication	-	-	-	-	-	-
Offshore Development	21	63	(42)	161	236	(75)
Corporate	(6)	2	(8)	4	6	(2)
Inter-Segment	5	(1)	6	(2)	(2)	-
Nalcor subtotal	826	852	(26)	3,424	3,286	138
Maritime Link - non-cash additions	(153)	(91)	(62)	(588)	(485)	(103)
Total capital expenditures, excluding Maritime Link	673	761	(88)	2,836	2,801	35

¹The breakdown of capital expenditures incurred related to LCP for the quarter is as follows:

<i>For the period ended December 31 (millions of dollars)</i>	Three months ended		Twelve months ended		Total To Date
	2017	2016	2017	2016	
Muskrat Falls	283	201	1,026	897	3,967
Labrador Transmission Assets	15	32	84	154	832
Labrador-Island Link	153	306	879	1,040	3,314
Nalcor facilities capital costs	451	539	1,989	2,091	8,113
Capitalized interest and financing costs ¹	62	45	238	173	746
Class B Limited Partnership Unit Interest	10	8	37	23	82
Transition to Operations	8	1	13	4	16
Total capital costs for Nalcor project components	531	593	2,277	2,291	8,957
Maritime Link	153	91	588	485	1,735
Total capital expenditures	684	684	2,865	2,776	10,692

¹Total to date excludes \$95 million of allowance for funds used during construction on Nalcor's Class A limited partnership units in the LIL LP that are eliminated upon consolidation.

For the three months ended December 31, 2017, capital expenditures, excluding Maritime Link were \$673 million as compared to \$761 million for the same period in 2016, a decrease of \$88 million. For the year ended December 31, 2017, capital expenditures, excluding Maritime Link were \$2,836 million as compared to \$2,801 million for the same period in 2016, an increase of \$35 million. The decrease for the quarter is due to lower expenditures in LCP Transmission, as construction of LTA and LIL assets is concluding and assets are preparing to transition to operations in 2018; a decrease in Oil and Gas capital expenditures, as Hebron entered into the production phase during the quarter; partially offset by an increase to capital expenditure in Muskrat Falls, as a result of continued construction. The increase for the year relates to the development of Muskrat Falls and the continuation of Hydro Regulated's capital program combined

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

with additional carry over capital work from 2016; partially offset by decreases in LCP Transmission as a result of the near completion of LTA and LIL assets and Oil and Gas due to the completion of Hebron.

OBLIGATIONS AND COMMITMENTS

Outstanding commitments for capital projects, excluding those related to Oil and Gas, total approximately \$1.0 billion as at December 31, 2017 (2016 - \$2.1 billion). LCP prefunded equity requirements associated with the Project Finance Agreements in Muskrat Falls and LCP Transmission total approximately \$1.0 billion as at December 31, 2017 (2016 - \$2.8 billion). Prefunded equity is used to fund capital and borrowing costs.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

SECTION 6: KEY BUSINESS RISKS

The following information describes significant risks inherent to Nalcor's activities. This section does not describe all applicable risks and is intended only as a summary of significant risks which could materially affect the business, results of operations and financial condition or cash flows. Other risks may arise or risks not currently considered to be material may become material in the future. The risks presented below are grouped by category and detail material operational, financial, regulatory, and compliance risks.

OPERATIONAL RISKS

Operational risks include risks to assets, other property, people and systems. This includes uncertainties relating to asset condition, maintenance and asset availability within the generation and transmission facilities that are maintained by Hydro, Churchill Falls and LCP; operational risks related to Nalcor's interests in oil and gas assets; risks related to the availability of transmission assets that Nalcor utilizes but does not own; as well as risks to other property and assets owned by Nalcor, such as office buildings, data, and system infrastructure.

Asset Condition and Maintenance Risk

Nalcor maintains a comprehensive corporate insurance program typical for such a company. Insurance is subject to coverage limits and exclusions, as well as time-sensitive claims discovery and reporting provisions, and will not be available for all the risks and hazards to which the Company is exposed. In addition, no assurance can be given that such insurance will be adequate to cover the Company's liabilities or will be generally available in the future, or if available, that premiums will be commercially justifiable.

Generation and Transmission Assets

Hydro and Churchill Falls' operations are subject to normal risks inherent to operating generation and transmission assets. Certain assets are approaching the end of their service lives and are becoming more costly to maintain. The occurrence of significant unforeseen equipment failures could have a material adverse effect on operations in these entities, as well as the cash flows and financial position of Nalcor, particularly considering the isolated nature of the provincial electrical system and growing demand on the Avalon Peninsula.

Hydro and Churchill Falls maintain integrated annual work plans which consolidate and monitor the activities within operating, capital, winter readiness and preventative and corrective maintenance programs. Utility assets are maintained in a manner that accounts for the age of the infrastructure and for the extreme weather conditions that are inherent to our climate.

Joint Venture Interest in Oil and Gas Assets

Oil and Gas is subject to the operational risks of participation in offshore oil production, including equipment defects, malfunctions, failures, unplanned shut downs, safety or environmental incidents and external factors, such as hurricanes, ice conditions and other extreme weather. These risks and hazards create exposure to events such as workplace incidents, business interruption, property damage or destruction, or environmental liabilities.

These operational risks are managed by the operator of projects in which Nalcor is a minority joint venture partner. The approach and performance of the operator with respect to addressing these areas is monitored actively by reviewing project status reports and risk registers, participation in meetings with co-venturers, and the exercise of Oil and Gas voting rights within operating agreements.

The occurrence of events described above could materially impact revenue assumptions, and/or unplanned capital work, or lead to other expenses requiring increased equity investment from partners.

Safety Risk

Several of Nalcor's lines of business have material inherent safety risks and related municipal, provincial and federal requirements with associated potential liabilities. Notably within utility operations, this includes risks relating to working around energized equipment and operating dams and dykes. There are additional unique hazards associated with certain facilities, such as the underground powerhouse at Churchill Falls. Construction sites, such as at LCP workplaces and those relating to various capital projects for Hydro and Churchill Falls, carry risks relating to working from heights, dropped objects, and management of contractors onsite.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Based on the industry and the nature of work performed, there are many hazards and risks that could result in workplace incidents that could cause serious injury or death to employees, contractors or members of the public. Safety events can lead to disruption of the business, regulatory actions, and other measures, which could have an adverse impact on the Company. Unsafe work conditions can lead to workplace incidents that may result in increased turnover, increased project and operating costs, and lead to additional unforeseen expenses to investigate and respond to such events.

Environmental Risk

Nalcor is subject to various municipal, provincial and federal requirements, and given the industry and nature of the work performed, there are a number of environmental risks that may adversely affect Nalcor's financial position in any given year. There is a potential for environmental liability with existing assets or from assets assumed from another operator, or the presence or release of hazardous or other harmful substances. It is also possible that planned work is affected by the lack or absence of government approvals, permits, or renewals of existing approvals and permits related to construction or operating facilities. Environmental events may cause significant environmental damage, lead to claims by third parties and/or governmental fines, disruption to operations, increased project or operating costs, orders or directives requiring specific actions with associated costs or cause long-term impairment to asset values.

Nalcor applies the principles of ISO 14001 Environmental Management System standard to its relevant lines of business, which is a risk based framework for managing significant environmental risks and reducing the frequency and severity of incidents. Nalcor and its affiliated companies have developed Environmental Emergency Response Plans to deal with any accidental releases which may occur in order to provide a quick and effective response so that any impacts are minimized.

Lower Churchill Project Execution Risk

As is the case with any large construction project, there are a variety of uncertainties relating to execution. There is a risk that costs can increase over original estimates and schedules can be impacted by a number of factors.

Factors impacting project capital costs and schedules are closely monitored. Organizational and structural changes implemented in 2016 separated the generation and transmission elements of the project and to allow for more focus on the completion of each scope of work. LCP maintains an owner controlled insurance program. Insurance is subject to coverage, limits and exclusions, as well as time sensitive claims discovery and reporting provisions. In addition, no assurance can be given that such insurance will be adequate to cover liabilities.

Offshore Oil Development Risk

The demand for, and pricing of, oil has a direct impact on the level of exploration, development and production activity in Newfoundland and Labrador's offshore region. This, and numerous other market conditions over which Nalcor has no control, may also impact results including commodity prices, expectations about future prices, levels of consumer demand, severe weather events, policy or regulatory change, economic conditions, and the ability of oil and gas companies to raise capital.

Any prolonged substantial reduction in oil and gas prices may slow the current pace of offshore oil exploration and development until market conditions are more favorable, and a prolonged and substantial increase may spur higher than expected interest and development.

Electricity System Integration Risk

LCP is under construction and the transmission interconnection between the isolated island grid to North America is planned for 2018 as both the Maritime Link and Labrador-Island Link are expected to be in service. The integration of Muskrat Falls and related transmission assets into the existing asset base is complex and involves a high degree of coordination. As such, the Company is focused on completion of LCP, system integration efforts and planning for the implementation of new operating procedures and commercial agreements.

Seasonality

Weather conditions, including abnormally warm or cold weather that causes higher or lower than expected energy usage for heating or cooling purposes or periods of low rainfall that impact economic operation of hydro assets, can have a material impact on cash flows and financial results, in particular for Hydro and Churchill Falls. Energy Trading, which exists to optimize excess power, may also be affected where seasonality patterns differ from normal ranges to an extent that it impacts demand and pricing in target sales markets. Despite preparations for severe weather, ice, wind and snow storms, hurricanes and other natural disasters, weather will always remain a risk to

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

the physical assets of utilities. Global warming and climate change may have the effect of increasing the severity and frequency of weather related natural disasters that could affect the Company's service territories. Unforeseen changes to energy consumption from changing temperature swings could affect expected seasonality and demand assumptions. Although physical utility assets have been constructed and are operated and maintained to withstand severe weather, there can be no assurance that they will successfully do so in all circumstances. Unforeseen capital investments may be required to respond, forecasts of water reservoir volumes and assumptions regarding design and engineering for extreme weather may change.

Catastrophic Event Risk

Other external factors exist, where their occurrence would be sudden and the impact catastrophic. This includes, but is not limited to, an act of terrorism against key generation or transmission infrastructure, a major cyber-attack targeting key systems, including those that operate generation and transmission assets, and a catastrophic natural disaster, such as a major hurricane or tsunami.

To mitigate the risk of a sudden and catastrophic incident, Nalcor has business recovery and other emergency preparedness measures and controls governing both physical and information technology security threats. To the extent that coverage is available, certain risks are transferred through the placement of insurance. Such events are unlikely, but could have severe, sudden and potentially long-term impacts on the Company.

Information Technology Infrastructure and Security Risk

Information technology affects all aspects of Nalcor's operations. The Company's success is in part dependent on developing, maintaining and managing complex IT systems which are employed to operate transmission and generation facilities, financial, and other business systems. If such systems are not robust or do not support the needs of the business, performance may be negatively impacted due to errors, poor efficiency and/or loss of system stability. To respond to aging business systems and changing needs of the Company, Nalcor is undergoing a comprehensive upgrade and replacement of key corporate business systems.

The business relies heavily on its corporate business systems for core activities and any disruptions in operations could potentially result in delays in issuing accurate internal or external reporting, including financial reports, as well as information required to maintain contractual and regulatory compliance. In addition, it could result in delays issuing vendor payments, processing payroll, or providing customer billings.

Increasing reliance on information systems and expanding data networks creates exposure to information security threats. Major risk exposures in this environment relate to information security, availability of information, and risk of corporate data loss. It also may include the loss of processing capability due to hardware and/or software failure or virus attacks, the loss of communication across the wide area network, the loss of data through cybercriminal malware, or similar events. There are unique risks relating to the industrial control systems and other operational technologies that control the electricity grid and certain physical assets. External threats are mitigated through the use of firewalls, anti-virus tools and detection and intrusion prevention appliances. Internet access is controlled and, where devices are connected, this is managed by a web-filtering device. Nalcor maintains a disaster recovery plan that details recovery procedures and processes, and is updated and tested on a periodic basis.

A serious incident involving the loss of corporate data or access to critical systems would result in unplanned costs to contain, investigate, and remediate the incident and may result in unplanned investments to change systems or processes. It could also result in the loss of control over physical assets, or inability to access corporate systems and data.

Human Resource Management Risk

The future success of Nalcor is tied to attracting and retaining sufficient qualified staff to replace those retiring. Approximately 20% of full time equivalent employees will be eligible for the earliest unreduced pension within the next five years. This is compounded by the integration of LCP assets, which creates challenges to attracting and retaining adequate numbers of specialized and experienced staff to manage existing assets, in particular the HTGS and various rural operations, while simultaneously recruiting sufficient numbers of skilled workers to support the operation of new infrastructure as it comes in-service.

A focused integrated workforce plan and recruitment strategy has been developed and Nalcor is developing internal processes to guide decisions, such as the timing of transfers, which considers risk and criticality to the overall business.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

The collective agreement with Churchill Falls IBEW Local 2351 is effective for the period from January 1, 2014 to December 31, 2018, and Newfoundland and Labrador Hydro IBEW Local 1615 is effective for the period from April 1, 2014 to March 31, 2018. There is ongoing preparation for collective bargaining and discussions taking place with IBEW locals.

Oil and Gas Production Volume Risk

As a partner in three offshore developments, Nalcor is largely dependent on the operators to manage the risks that are associated with production and development. In addition to operating risks, commodity price and foreign exchange risk, Oil and Gas is subject to volume risk, or fluctuations in production levels. Decisions may be made by the operator that may adversely affect project production levels if they are in the best interest of the life of specific development projects. Given the early stage of Nalcor's growth in the oil and gas sector, Nalcor is not yet diversified, holding interests in only three producing projects. Nalcor maintains a very close working relationship with the operator of each of these ventures, has influence over key decisions made through joint venture rights and obligations, and actively participates in the various executive and operating committees.

The impact of unanticipated declining production in one well in either project could have a significant adverse effect on Nalcor's results and financial position.

Transmission Constraints Risk

Transmission constraints are relevant to the lines of business that operate in electricity markets either generating or selling power, and can result from high demand on transmission assets into key markets. For energy marketing activities, risks relating to transmission constraints are managed to the extent possible through firm contractual arrangements securing the use of transmission infrastructure, combined with the purchase of financial products mitigating the risk due to line congestion into key markets.

Limitation of Internal Control Systems

Management is responsible to ensure that risks are controlled by putting in place and monitoring processes and systems designed to reduce such risks as detailed above. Internal control systems are intended to provide reasonable assurance with respect to the achievement of objectives, and those controls deemed to be effective do not eliminate the risk altogether. They may not always prevent or detect misstatements with respect to financial statement preparation and presentation, or prevent material financial losses from occurring.

FINANCIAL RISK

Nalcor's operations create exposure to various forms of financial risk including commodity price, foreign exchange, credit, and liquidity risk. Financial risks are managed in accordance with a Board-approved Financial Risk Management Policy. Board approval is required whenever derivative instruments are used to hedge against an identified financial risk.

Commodity Price Risk

Commodity price risk arises wherever a change in the market price for a particular commodity would cause a corresponding change to expected profit, cash flow and/or the fair value of assets/liabilities. Nalcor's primary exposure to commodity price risk is through the sale of crude oil by Oil and Gas; the purchase of No. 6 fuel, gas turbine fuel, and diesel fuel for Hydro Regulated thermal facilities; and the sale of recall power by Energy Trading. Within Hydro Regulated, regulatory recovery mechanisms are available which provide certainty that profit will not be affected by movements in commodity price relating to the purchase of No. 6 fuel, diesel and gas. For oil sales and recall power sales however, profit is sensitive to market price fluctuations. The market price for electricity is impacted by a number of factors including the impact of other existing and emerging technologies for the generation of electricity. Assuming no risk mitigation, with all other variables and assumptions held constant and regarding anticipated volumes sold in 2018, an increase (decrease) of \$1 in the average Dated Brent price (USD/bbl) will impact profit in Oil and Gas by \$1.7 million. A \$1 increase (decrease) in the average electricity export price (USD/MWh) will affect profit in Energy Trading by \$1.0 million.

When considered appropriate in the context of the Company's financial management objectives, management will use fixed price commodity price swaps to reduce the impact of commodity price volatility and create cash flow certainty. At the beginning of 2018, Oil and Gas had 4 swap contracts in place with a notional value of \$97.9 million USD. These contracts provide an average price of \$61.36 USD on 1,595,796 barrels of 2018 production. Energy Trading had 2 swap contracts in place with a total notional value of \$4.4 million

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

USD. These contracts effectively lock in an average price of \$43.84 USD per MWh on 100,975 MWh of anticipated 2018 exports to New England.

Hydro Regulated's exposure to the impact of commodity price fluctuations through the purchase of No. 6 fuel is mitigated by the operation of the RSP which passes commodity price risk on fuel purchases to customers. Hydro has obtained approval from the PUB to defer fluctuations in the price of diesel and gas turbine fuel which reduces the impact of this volatility on profit. However, the PUB has yet to issue a decision on whether the balances in the diesel and gas turbine fuel amounts will be recovered by Hydro Regulated. Therefore, while the RSP and the diesel and gas turbine deferral accounts can mitigate the impact of fuel price volatility on profit, neither account removes the effect of such volatility on cash flows, which is managed by ensuring sufficient short term liquidity is available to address unexpected and significant increases in fuel purchases.

Foreign Exchange Rate Risk

Foreign exchange rate risk arises when a financial transaction is denominated in a currency other than that of the base currency of the Company, being CAD. Nalcor's primary exposure to foreign exchange rate risk arises from exposure to USD through the sale of crude oil by Oil and Gas, Hydro Regulated's purchases of No. 6 fuel for consumption at the HTGS and the sale of recall power at USD market rates by Energy Trading. As is the case for commodity price exposures relating to Hydro Regulated's purchase of No. 6 fuel, regulatory recovery is permitted relating to foreign exchange rate impacts as described in further detail below. For oil sales and recall power sales, profit is sensitive to fluctuations in the USD/CAD exchange rate. Assuming no risk mitigation, with all other variables and assumptions held constant and regarding anticipated volumes sold in 2018, a change of \$0.01 in the average USD/CAD rate represents an annual increase (decrease) in profit of \$0.8 million for Oil and Gas. The same change in foreign exchange rate translates to an annual impact of \$0.1 million to the profit of Energy Trading.

When considered appropriate in the context of the Company's financial management objectives, management will use forward contracts to reduce the impact of foreign exchange rates on profit and create cash flow certainty. At the beginning of 2018, Oil and Gas and Energy Trading had forward contracts in place which effectively provide an average rate of \$1.28 CAD per USD on \$100.6 million USD and \$9.7 million USD of 2018 USD revenue, respectively.

Hydro's foreign exchange exposure on the purchase of No. 6 fuel is mitigated through the operation of the RSP which transfers the effects of foreign currency changes on fuel purchases to customers. The regulatory framework for the rate-regulated business allows for recovery of prudently incurred costs, including those relating to changes in foreign exchange rates. While the RSP can mitigate the impact of currency volatility on profit, it does not protect against the effect of such volatility on cash flow. This is managed by ensuring sufficient short term liquidity is available to address unexpected and significant increases in fuel purchases.

Credit Risk

Credit risk represents the financial loss that would be suffered if the Company's counterparties in a transaction fail to meet or discharge their obligation to the company. Nalcor is exposed to credit risk in the event of non-performance by counterparties to its financial instruments or in non-performance of suppliers and/or contractors.

Credit risk relating to the revenues in Churchill Falls and Hydro Regulated are largely mitigated by the profile of its customers, who are typically regulated utilities or investment grade counterparties, which are designated as low risk. Procedures and practices designed to manage the credit risks include assessment and monitoring of counterparty creditworthiness, setting of credit limits, monitoring collections, and maintenance of various forms of credit assurance, including letters of credit, performance bonds and parental guarantees as part of the terms of final contracts. Credit risk related to the sale of recall power and crude oil is managed through contractual arrangements with counterparties assessed to be creditworthy, supported by credit enhancements as required.

Investments are similarly restricted to high-quality securities. Investments held within the sinking fund portfolios of Nalcor and Hydro Regulated and the reserve fund in Churchill Falls are limited to securities issued by or guaranteed by the Government of Canada, any of the provincial governments and Canadian banks rated A or better by Standard and Poor's (S&P's). In addition, portfolio investments held within the reserve fund of Churchill Falls do not exceed 10% with any one entity with the exception of the Government of Canada. Long-term investments held by Muskrat Falls, Labrador Transco, and the LIL Construction Project Trust are with a Canadian Schedule 1 Bank with a credit rating of A (S&P's). Derivative transactions are executed with only highly rated banking institutions.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Default by a company that Nalcor has extended significant credit to could result in material lost revenue, increases to bad debt expense, and a negative impact to Nalcor's statement of financial position as receivables are deemed to be uncollectible.

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. Nalcor is exposed to liquidity risk with respect to its short-term contractual obligations and financial liabilities. Short-term liquidity is provided by cash and cash equivalents, funds from operations and maintenance of borrowing facilities sufficient to cover both anticipated and unexpected fluctuations within its operations. Cash flows are monitored continuously. The Company maintains a \$250 million committed credit facility with its bank to ensure additional liquidity is available to each of the lines of business. In addition, Hydro Regulated maintains a \$200 million committed credit facility and demand operating credit facilities are maintained for Oil and Gas, Churchill Falls and Energy Trading with limits of \$30 million, \$10 million and \$20 million, respectively.

Historically, Hydro Regulated addressed longer-term capital funding requirements by issuing government guaranteed long-term debt in the domestic capital markets. However, in December 2017, Hydro Regulated changed its process to one whereby the Province issued debt specifically on Hydro Regulated's behalf and lends the proceeds to Hydro Regulated on a cost recovery basis. Long-term liquidity is also provided through injections of equity capital from the Province in support of the existing large project investments. Long-term liquidity depends on Hydro Regulated's continued ability to access the capital markets and on Nalcor's shareholder's ability to provide required equity contributions. The funding obligations associated with the longer-term debt is managed through a balanced approach to debt maturity and a program of sinking fund investment. Debt maturities are managed to avoid overly demanding funding requirements in any given year.

Diminished liquidity may result in constraints on executing growth plans and carrying out planned investments and acute shortages could negatively affect the organization's ability to operate.

Key Estimates Risk

Nalcor is subject to uncertainty pertaining to key estimates and assumptions including, but not limited to, changes in crude oil production and electricity generation and/or sales levels and prices, particularly relating to revenue, and potentially impacting all affiliated companies. Where financial and operating assumptions are required, various scenarios are considered to account for the possibility that actual conditions differ from those expected. However, reasonable assumptions must be selected and financial results and operating conditions may be materially impacted during periods where external factors are outside the normal expected range.

Carbon Tax Risk

The consideration of Federal and Provincial carbon taxes may create financial opportunities and risks for the Company going forward, as taxes are reasonably expected to increase for fuel burning facilities but having a generation mix that is predominantly hydro power may make our renewable electricity more desirable as it is not expected to be taxed. Environmental teams liaise with federal, provincial, municipal and state regulators and the potential impacts on operations and infrastructure are considered within the established environmental risk management framework.

Sustainability of Future Electricity Rates

Since LCP was sanctioned, several key assumptions have changed, namely the cost of construction. Additionally, load forecasts and required supply assumptions have decreased from levels expected in 2012. Projected electricity rates have increased from initial estimates, and there are concerns that the projected rates are not sustainable. In addition, projected rates may cause uncertainty on cash flows and asset valuations and may incent customers to take conservation measures and demand side management actions, further increasing rates. Nalcor is currently reviewing, in coordination and consultation with the provincial government, any available options for reducing future electricity rates for the ratepayers of the Province.

REGULATORY RISK

Hydro Regulated is subject to the normal uncertainties facing entities that operate under cost of service rate regulation, including approvals by the PUB. The PUB approves electricity rates charged to Hydro Regulated's customers and ensures that those same rates provide Hydro Regulated with a reasonable opportunity to recover the estimated costs of providing electrical services, including a fair rate of return on rate base.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

While Hydro Regulated can make applications to the PUB for recovery of capital projects, there is no assurance that these projects will be approved in part or in full, or that conditions on such approvals will not be imposed. Further, there is no assurance that Hydro Regulated will receive regulatory decisions in a timely manner, meaning costs may have to be incurred prior to having approval of recovery from customers. Finally, there is no assurance that rate orders issued by the PUB will permit Hydro to recover all costs actually incurred to provide electricity service. Management works to mitigate these risks by ensuring both compliance with existing regulations and the proactive management of regulatory issues.

In total, the uncertainties inherent to the regulatory process governing the operation of Hydro Regulated may negatively affect the timing of capital projects, results of operations and financial position of Nalcor if significant in nature.

COMPLIANCE RISK

Legislative Compliance

In addition to environmental and occupational, health and safety requirements, Nalcor's operations are subject to a variety of other federal, provincial, and local laws, regulations and guidelines, including market rules governing Energy Trading, provincial royalties and other regulations relating to the province's interest in offshore oil projects, federal aviation regulations concerning the operation of Churchill Falls airport, privacy and other various employment laws. Certain legal issues are managed by Nalcor's corporate legal team, but most compliance risks are managed by the affiliated company they relate to.

As Nalcor grows its Energy Trading segment and interconnects the island to the North American electrical system, it is subject to increasing levels of United States and Canadian regulation and market participant rules. This introduces the risk of loss of authorizations necessary to participate in chosen export markets in reaction to noncompliance. Such occurrences may affect the Company's ability to meet sales and other targets. Management has established dedicated resources to develop and maintain an appropriate compliance framework.

In certain instances, the outcome of noncompliance may have material impacts on revenue assumptions, cash flows or expenses, or may affect the timely delivery of a product, service, or project in a given period.

Contractual Compliance

Nalcor has contracts in place with various related companies and third parties including, but not limited to, arrangements relating to federally guaranteed debt and power purchase agreements governing the sale of power. Across all segments, there are agreements relating to revenue generation activities, financing of key investments and projects, the delivery of power and other products and services, the use of Nalcor sites or locations by third parties, and the payment of various contractors and service providers. Contracts are awarded in compliance with provincial purchasing requirements and regulation, as well as Nalcor internal purchasing guidelines, and standard contracts are often used.

Default by Nalcor relating to a material contract, or default of another party to key agreements may affect the Company's ability to meet sales or other targets as well as fund or deliver major capital projects. From time to time, disputes arise between Nalcor and related or third parties which create uncertainty with respect to various financial targets affected by certain contracts with the potential to be material.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

SECTION 7: ACCOUNTING POLICIES AND SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUMPTIONS

CURRENT AND FUTURE CHANGES IN ACCOUNTING POLICIES

In 2017, there were no new or revised accounting standards adopted that had a material impact on the consolidated financial statements of Nalcor.

As new standards, amendments and interpretations are issued, Nalcor assesses the potential impact of the changes on its financial statements prior to the effective date. The following new standards, amendments and interpretations have been issued by the IASB, but are not yet effective and have not been implemented. Nalcor is currently reviewing the potential impact of these standards on its consolidated financial statements and does not intend to early adopt any of the following standards.

Financial Instruments: IFRS 9

IFRS 9 was issued in July 24, 2014 to supersede IAS 39 – Financial Instruments: Recognition and Measurement upon its effective date of reporting periods commencing on or after January 1, 2018, with earlier application permitted. The revised standard contains requirements for the classification and measurement of financial instruments, impairment, derecognition and general hedge accounting. Under the new standard, the categories for classification of financial assets will be reduced as all financial assets currently within the scope of IAS 39 will be subsequently measured at either amortized cost or fair value. Changes in the credit risk of financial liabilities measured at fair value will be presented in other comprehensive income versus profit and loss.

The standard introduces a new forward looking impairment model for measurement of credit losses based on expected losses as opposed to incurred losses. The new model is designed to result in earlier recognition of credit losses and to consider a broader range of reasonable supportable information to inform credit loss estimates.

Under the revised standard there will be greater flexibility for hedge accounting, as the effectiveness test will be based on the qualitative economic relationship of the hedging instrument and hedged item versus a quantitative retrospective assessment of effectiveness. Additional disclosure requirements have also been added surrounding the risk management activities of the entity. Management has assessed and although there will be changes to classification of existing financial instruments and related disclosures, there will be no material adjustments to amounts reported in Nalcor's consolidated financial statements.

Revenue from Contracts with Customers: IFRS 15

IFRS 15 was issued on May 28, 2014, and will replace IAS 18 – Revenue and IAS 11 – Construction Contracts, along with several Interpretations related to revenue upon its effective date of periods commencing on or after January 1, 2018, with earlier application permitted. The standard specifies how and when to recognize revenue and requires entities to provide more informative, relevant disclosures. Management has assessed and although there will be changes to related disclosures, there will be no material adjustments to amounts reported in Nalcor's consolidated financial statements.

Foreign Currency Transactions and Advance Consideration: IFRIC 22

IFRIC 22 was issued to address how to determine the 'date of transaction' for the purpose of determining the exchange rate to use on initial recognition of an asset, expense or income, when consideration in a foreign currency has been paid or received in advance, resulting in a non-monetary asset or liability. The Interpretation is effective for periods starting on or after January 1, 2018 with earlier application permitted. The application of this Interpretation will not have a material impact on Nalcor's consolidated financial statements.

Leases: IFRS 16

IFRS 16 was issued on January 13, 2016, to supersede IAS 17 – Leases along with a number of Interpretations, upon its effective date of periods commencing on or after January 1, 2019, with earlier application permitted. The standard provides a comprehensive model for the identification of lease arrangements and their accounting treatment. The greatest impact of this new standard is the requirement for lessees to record assets and liabilities on the statement of financial position for all leases, not just finance leases, with some exceptions such as short term leases and low value leases. Treatment of leases for lessors will remain relatively unchanged. Management anticipates that the application of this standard in the future may have a material impact on the amounts and disclosures reported in Nalcor's consolidated financial statements. However, it is not practicable to provide an estimate at this time as Management is still conducting a detailed review.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Nalcor's significant accounting policies are described in Note 2 of the consolidated annual financial statements. Several of these policies involve balances or transactions which require significant accounting judgments, estimates and assumptions that impact reported amounts of assets, liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amount of revenues and expenses during the reporting periods. Significant accounting estimates and judgements are described in Note 3 of the annual consolidated financial statements and are based on historical experience, current conditions and various other assumptions believed to be reasonable under the circumstances. Due to changes in facts and circumstances, and the inherent uncertainty involved in making estimates, actual results may differ materially from current estimates. The estimates and assumptions used are reviewed on an on-going basis by Management and, as adjustments become necessary, are recognized in profit or loss in the period in which they become known. A summary of Nalcor's critical accounting estimates are as follows:

Revenue

Revenue recorded in Hydro Regulated includes unbilled electricity consumed by retail customers during the period. Determining the value of the unbilled consumption involves an estimate of consumption for each retail customer based on the customer's consumption history in relation to key inputs such as current price of electricity, economic activity, weather conditions and system losses. The estimation process for unbilled electricity will result in adjustments to revenue in the periods they become known, when actual results differ from estimates.

Regulatory Adjustments

Regulatory assets and liabilities recorded in Hydro Regulated arise due to the rate-setting process for regulated utilities governed by the PUB. The amounts relate to costs or credits which Management believes will be recovered or settled through customer rates in future periods, pursuant to the proceedings and outcomes of future PUB orders. Certain estimates are necessary since the regulatory environment often requires amounts to be recognized at estimated values until these amounts are finalized pursuant to regulatory decisions or other regulatory proceedings. The final amounts approved by the PUB for deferral as regulatory assets and regulatory liabilities and the approved recovery or settlement periods may differ from those originally expected. Any resulting adjustments to original estimates could have a material impact and are recognized in profit or loss in the period in which they become known. In the event that a regulatory decision is received after the balance sheet date but before the consolidated financial statements are issued, the facts and circumstances are reviewed to determine whether or not it is a recognized subsequent event.

As at December 31, 2017, Hydro Regulated recognized a total of \$117 million in regulatory assets (2016 - \$164 million) and \$79 million in regulatory liabilities (2016 - \$348 million). For further detail of regulatory assets and liabilities please refer to Note 12 to Nalcor's consolidated annual financial statements.

Depreciation, Depletion and Amortization

Depreciation, depletion and amortization are significant estimates included in the Nalcor consolidated financial statements due to the significant asset balances carried in property, plant and equipment and intangible assets. As at December 31, 2017, Nalcor's consolidated property, plant and equipment and intangible assets are \$15 billion, or approximately 81% of total consolidated assets compared to \$11 billion or approximately 82% of total consolidated assets as at December 31, 2016. Total depreciation, depletion and amortization is \$168 million for the year ended December 31, 2017 (2016 - \$135 million).

Depreciation is recorded on a straight line basis over the useful lives as determined by independent specialists while amortization is recorded on a straight line basis over the useful lives as determined by Management. These useful lives are Nalcor's best estimate and are reviewed annually by Management. Any change in these estimates could materially affect the amount of depreciation or amortization recorded. For Hydro Regulated, depreciation and amortization are approved by the PUB. The depreciation periods used and associated rates are reviewed on an ongoing basis to ensure they continue to be appropriate. From time to time, third party depreciation studies are performed, and based on the results of these depreciation studies, the impact of any over or under depreciation as a result of actual experience differing from that expected and provided for in previous depreciation rates is generally reflected in future depreciation rates and depreciation expense, when the differences are refunded or collected in customer rates, as approved by the regulator.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

Depletion is determined using the unit of production method based on actual production and oil and natural gas reserves, as evaluated by independent reserve engineers. Estimates of recoverable reserves are based upon variable factors and assumptions regarding historical production, production rates, ultimate reserve recovery and timing and amount of future cash outflows. Changes to the ultimate reserve recovery and timing and amount of future cash outflows can have a material impact on this calculation.

Impairment of Non-Financial Assets

Non-financial assets are assessed for indicators of impairment at the end of each reporting period. Non-financial assets are impaired where there is evidence that, as a result of one or more events that occurred after the initial recognition of the non-financial asset, the recoverable amount of the asset has been impacted. Where it is not possible to estimate the recoverable amount of an individual asset, Nalcor estimates the recoverable amount of the cash generating unit (CGU) to which the asset belongs. The determination of a CGU requires judgement in determining the level at which cash flows are largely independent of other assets or groups of assets. Management uses internal qualitative and quantitative assessments. The calculation of recoverable amount includes a discounted cash flow analysis which may include estimates and assumptions regarding expected future revenue often driven by commodity prices and volume, the timing and amount of future operating and capital cash flows and a market participant discount rate. The calculation of the recoverable amount of a CGU also requires judgement surrounding future events. Changes to these estimates can have a material impact on this calculation and while no impact on cash flows, can lead to large fluctuations in profit or loss between reporting periods. For the year ended December 31, 2017, the impact of asset impairments on Nalcor's profit or loss was \$132 million (2016 - \$nil). Impairment in 2017 relates to costs associated with exploration intangible assets and certain older costs related to Gull Island project assets, which Management anticipates no longer have future economic benefit.

Partnership Unit Liabilities

Partnership unit liabilities represent the limited partner's ownership interests in the Partnership based on the fair value of the Class B limited partnership units at each reporting date. Due to the nature of the liability and the lack of comparable market data, the fair value is determined using the present value of future cash flows. Significant assumptions are used in the calculation including the amount and timing of future cash flows and the discount rate. As at December 31, 2017, the carrying value of the Class B limited partnership units on the statement of financial position is \$491 million (2016 - \$399 million).

Decommissioning Liabilities

Decommissioning liabilities are recorded to recognize a liability for the fair value of the future expenditures required to settle obligations associated with the retirement of property, plant and equipment. Significant assumptions and estimates surrounding the timing and amount of future cash flows required to settle obligations, along with the discount rate, are used to determine the fair value of the liability. Measurement requires making reasonable estimates concerning the method of settlement and settlement dates associated with legally obligated decommissioning costs. There are uncertainties in estimating future decommissioning costs due to potential external events such as changing legislation or advances in remediation technologies. Changes to the amount or timing of the settlement cash flows can have material impact on the calculation. Nalcor has decommissioning liabilities associated with the retirement of portions of the HTGS, disposal of Polychlorinated Biphenyls (PCB) and from its net ownership interests in petroleum and natural gas properties and related well sites.

A significant number of Nalcor's assets include generation plants, transmission assets and distribution systems. These assets can continue to run indefinitely with ongoing maintenance activities. As it is expected that these assets will be used for an indefinite period, no removal date can be determined and consequently, a reasonable estimate of the fair value of the cost of decommissioning liability cannot be determined at this time. If it becomes possible to estimate the fair value of the cost of removing assets that Nalcor is required to move, a decommissioning liability for those assets will be recognized at that time.

Decommissioning liabilities are periodically reviewed by Management and any changes are recognized as an increase or decrease in the carrying amount of the liability and the related asset. As at December 31, 2017, Nalcor's decommissioning liabilities were \$86 million (2016 - \$83 million).

Employee Future Benefits

Employee future benefits, which consist of group life insurance and health care benefits, are provided to retired employees on a cost-shared basis, in addition to a retirement allowance. The expected cost of providing these benefits is actuarially determined by an

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

independent actuary using Management's best estimate of salary escalation, retirement ages of employees and expected health care costs. Changes in the assumptions such as the discount rate, inflation rate, and life expectancy, along with the estimates of salary, retirement and health care costs could have a material impact on the liability. As at December 31, 2017, Nalcor's total employee future benefits liability is \$126 million (2016 - \$117 million).

Contingencies

Nalcor and its subsidiaries are subject to various legal proceedings and claims associated in the normal course of business operations. Management believes that the amount of liability, if any, from these actions would not have a material adverse effect on Nalcor's consolidated financial position, results of operations or cash flows.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

SECTION 8: NON-GAAP FINANCIAL MEASURES

Certain financial measures in the MD&A are not prescribed by GAAP. These non-GAAP financial measures are included because they provide MD&A users with enhanced understanding and clarity of Nalcor's financial performance, condition, leverage and liquidity. These non-GAAP financial measures do not have any standardized meaning and cannot necessarily be compared to similar measures presented by other companies.

NON-GAAP FINANCIAL MEASURES

Debt to capital	Total debt (short-term borrowings, long-term debt including current portion less sinking funds and Class B limited partnership units), divided by total debt plus shareholder's equity
EBIT	Profit (loss) excluding interest and taxes
EBITDA	Profit (loss) excluding interest, taxes, depreciation, depletion, amortization, impairment and accretion
Fixed rate debt as a percentage of total indebtedness	Long-term debt including current portion, divided by total debt
Funds from operations (FFO)	Profit (loss) excluding depreciation, depletion, amortization, impairment and accretion
Return on capital employed (ROCE)	Rolling twelve month average EBIT (excluding impairment)/Capital Employed (total assets, excluding assets that are under development)

Disclosure of Operating Profit (Loss)

The term "operating profit (loss)" is a non-GAAP measure that encompasses profit (loss) excluding extraordinary and non-recurring items that are not indicative of Nalcor's future financial performance. This non-GAAP financial measure provides a more accurate reflection of Nalcor's operating performance and analysis against prior periods.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

SECTION 9: RELATED PARTY TRANSACTIONS

Nalcor enters into various transactions with its shareholder and other affiliates. These transactions occur within 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 Nalcor transacts are as follows:

Related Party	Relationship
The Province	100% shareholder of Nalcor
Churchill Falls	Joint arrangement of Hydro
Hydro-Québec	34.2% shareholder of Churchill Falls
Twin Falls	Joint venture of Churchill Falls
Churchill Falls (Labrador) Corporation Trust (The Trust)	Created by the Province with Churchill Falls as the beneficiary
LIL LP	Partnership in which Nalcor holds 75 Class A Partnership Units, 1 Class C Partnership Unit and 1 General Partner Unit
PUB	Agency of the Province

Routine operating transactions with related parties are settled at prevailing market prices under normal trade terms. Outstanding balances due to or from related parties are non-interest bearing with no set terms of repayment, unless otherwise stated. For additional information and detail on related party transactions refer to Note 31 in the annual consolidated financial statements.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

SECTION 10: SUMMARY OF QUARTERLY RESULTS

The following table outlines Nalcor's quarterly results for the eight quarters ended March 31, 2016 through December 31, 2017. The quarterly information has been obtained from Nalcor's unaudited condensed consolidated interim financial statements. These financial results are not necessarily indicative of results for any future period and should not be relied upon to predict future performance.

<i>For the period ended (millions of dollars)</i>	Revenue	Profit (loss)	ROCE (%) ¹	FFO	Capital Expenditures ²
December 31, 2017	265	(94)	7.2%	86	673
September 30, 2017	159	22	9.9%	63	820
June 30, 2017	226	78	10.5%	121	795
March 31, 2017	280	57	8.6%	100	548
December 31, 2016	227	62	7.9%	103	761
September 30, 2016	155	37	6.7%	75	863
June 30, 2016	180	9	4.7%	42	719
March 31, 2016	263	28	4.7%	60	458

¹ Excludes assets under development

² Excludes Maritime Link

The financial performance of several of Nalcor's business segments are impacted by seasonality. Specifically, electricity sales in Hydro Regulated and Churchill Falls are typically highest during the first and last quarters and lowest during the summer months. In contrast, Energy Trading has the highest level of energy available to sell in export markets during the summer months and the least available to sell in winter months. Electricity prices in the export markets tend to peak in winter and summer periods, but can vary by year depending on temperatures, the specific market and other factors. Interim results can also fluctuate due to the timing and recognition of regulatory decisions and the impact of commodity price changes.

December 2017/December 2016

2017 fourth quarter profit (loss) decreased \$156 million compared to the same period in 2016, largely due to impairment expenses related to the exploration intangible assets and Gull Island project costs; an increase in operating costs primarily related to the CDA; an increase in depreciation and depletion in Hydro Regulated and Oil and Gas; losses on disposal of assets in Oil and Gas associated with the conclusion of Hebron construction; increased production, marketing and transportation costs in Oil and Gas; and the impact of timing of the recognition of 2016 cost deferrals in Hydro Regulated. The decrease was partially offset by higher oil revenue due to increases in volume and average Dated Brent prices.

September 2017/September 2016

2017 third quarter profit decreased by \$15 million compared to the same period in 2016, largely due to lower revenue in Hydro Regulated; reduced revenue in Energy Trading as a result of lower average export electricity prices; the write-down of assets resulting from the settlement agreement in Hydro Regulated; increased operating expenses; higher depreciation and amortization in Hydro Regulated and Oil and Gas; higher depletion associated with increased production in Oil and Gas; and losses on disposal in Oil and Gas associated with the conclusion of Hebron construction. These decreases were partially offset by higher oil revenue as a result of increased production and higher oil prices as well as decreased RSP interest in Hydro Regulated.

June 2017/June 2016

2017 second quarter profit increased by \$69 million compared to the same period in 2016, largely due to higher oil revenue as a result of increased production and higher oil prices; the recognition of a one-time adjustment to the Bull Arm Fabrication lease revenue related to the close-out value of the EMCP sublease agreement; and favourable regulatory adjustments in Hydro Regulated associated with the conclusion of the GRA. These increases were partially offset by higher depletion associated with increased production in Oil and Gas; higher depreciation and amortization in Hydro Regulated and Oil and Gas; losses on disposal in Oil and Gas associated with the conclusion of Hebron construction; and lower gains on settlement of oil commodity contracts.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

March 2017/March 2016

2017 first quarter profit increased by \$29 million compared to the same period in 2016, largely due to higher oil revenue resulting from increased production and higher realized oil prices compared to the same period in 2016. In addition, Energy Trading experienced higher prices and volumes related to export sales, while Hydro Regulated contributed to the increase in profit as a result of a reduction in gas turbine fuel expense as well as recognition of the prudence Order in Q1 2016. These increases were partially offset by higher depletion and production costs associated with increased production in Oil and Gas, higher depreciation and amortization in Hydro Regulated and Oil and Gas, increases in other fuel costs in Hydro Regulated, lower unrealized gains on commodity contracts in Energy Trading, lower realized gains on commodity contracts in Oil and Gas and reduced revenue in Churchill Falls as a result of the impact of the Renewal Contract.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

SECTION 11: SUBSEQUENT EVENT

On March 8, 2018, the Province issued long-term debt with a face value of \$300.0 million, specifically on Hydro's behalf. The debt matures on October 17, 2048 with a coupon rate of 3.70% paid semi-annually. Nalcor expects to use a portion of the proceeds to repay the \$225.0 million promissory note to the Province.

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

SECTION 12: OUTLOOK

On July 28, 2017, Hydro Regulated filed a new General Rate Application to set new rates for 2018 and 2019. The GRA process is expected to continue throughout 2018. Due to the timing of when the GRA is anticipated to conclude, new rates will not be in place for January 1, 2018. The recovery of the requested revenue requirement for the period in 2018 before new rates are implemented will be addressed through the GRA process in 2018. Timing and certainty of new rates is subject to PUB approval.

Once the Labrador-Island Link (LIL) is in service, and prior to the completion of the Muskrat Falls hydroelectric facility, Hydro Regulated will be able to direct Recapture to the island to service load, thereby displacing fuel consumption at its Holyrood thermal plant. Hydro Regulated has applied to establish a deferral account starting in 2018 which will include fuel savings and costs associated with these off-island purchases, with net savings being set aside for the benefit of customers. The proposed deferral account will include savings from the use of Recapture by Hydro Regulated that was previously sold to Energy Trading for export into external markets. As a result, 2018 forecasted profit for Energy Trading is anticipated to be significantly lower than previous years, as a portion of Recapture volumes previously sold in export markets will now be utilized by Hydro Regulated. While maintaining its focus on maximizing the export value of the remaining surplus Recapture, Energy Trading will also be working with Hydro Regulated during this period to procure market energy to further displace fuel consumption at Holyrood to the extent economically feasible. Energy Trading will continue efforts to optimize and secure market access for future Muskrat Falls exports.

Oil price continues to be volatile and any significant price change for 2018 unhedged production will impact profitability. To mitigate exposure on realized oil prices, Oil and Gas has entered into commodity price swaps providing an average fixed price of \$61.36 USD per barrel on approximately 1,600,000 barrels which represents 50% of budgeted 2018 production. Given that oil sales are denominated in USD, Oil and Gas has also entered into foreign exchange forward contracts with an average rate of \$1.28 CAD per USD and a notional value of \$97.9 million USD representing 50% of budgeted USD oil revenue.

Bull Arm Fabrication is forecasting a reduction in profit in 2018 compared to 2017 primarily related to the recognition in 2017 of the one-time adjustment of approximately \$26M to lease revenue related to the close-out value of the ECMP agreement as well as having no tenant currently in place for 2018. Management is evaluating opportunities through the RFP process with the goal of securing a tenant in the near future.

To mitigate price fluctuations on export market sales, Energy Trading has entered into commodity contracts with a notional value of \$4.4 million USD on 11% of 2018 anticipated Recapture volume at an average rate of \$43.84 USD. To mitigate foreign exchange fluctuations on USD sales, Energy Trading has entered into foreign exchange contracts with a notional value of \$9.7 million USD on 36% of 2018 budgeted USD sales at an average rate of \$1.28 CAD per USD.

Total capital expenditures for 2018 (excluding those related to the Maritime Link) are forecasted to be \$1.9 billion, a significant reduction from 2017 as the LCP Transmission and Muskrat Falls assets are moving out of the higher construction period as they move towards in-service.

Prior to expected first commercial power in 2020, significant components of transmission assets associated with LCP are anticipated to be completed and brought into service, at a limited capacity. Management is currently assessing the impact that this may have on financial results, as early as 2018.

Provincial legislation requires that the costs related to LCP be fully recovered from customer rates. Management continues to work with the Province to explore a range of potential strategies to mitigate the impacts on future customer rates. Until final decisions on rate mitigation are made, any potential impacts on Nalcor's future net income, cash flows, or asset impairment cannot be determined.

2018 will be a significant transitional year for Nalcor, with key changes in the business taking place. A portion of Nalcor's larger investments will move from the development phase to the testing/operations phase. These assets include LTA, LIL and Maritime Link. The Bull Arm Fabrication lease with ExxonMobil has concluded, resulting in Bull Arm Fabrication seeking new tenants for the site. Finally, energy will be delivered from Labrador to the Island for the first time using the LTA and LIL transmission assets. Hydro Regulated will be using a portion of the energy typically sold to export markets to supply Island requirements. As a result of these changes, capital

MANAGEMENT'S DISCUSSION & ANALYSIS

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2017

expenditure and net income levels will start to reduce in 2018 compared to 2017 levels. The anticipated income reduction is due primarily to a reduction in Bull Arm Fabrication's net income, operating and financing costs related to new transmission assets, and use of a portion of Recapture power to create an off-island purchases deferral account in Hydro Regulated.

APPENDIX 2



NALCOR ENERGY
CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2017

Independent Auditor's Report

To the Lieutenant-Governor in Council, Province of Newfoundland and Labrador

We have audited the accompanying consolidated financial statements of Nalcor Energy, which comprise the consolidated statement of financial position as at December 31, 2017, and the consolidated statements of profit and comprehensive loss, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Managements Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

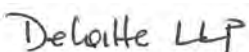
Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Nalcor Energy as at December 31, 2017 and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.



Chartered Professional Accountants
March 8, 2018

NALCOR ENERGY

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at December 31 (millions of Canadian dollars)

Notes

2017

2016

ASSETS

Current assets

Cash and cash equivalents	5	143	143
Restricted cash		1,037	1,378
Short-term investments	10	1,052	91
Trade and other receivables	6	395	294
Inventories	7	116	93
Current portion of other long-term assets	11	2	82
Prepayments		20	16
Derivative assets		3	1
Total current assets		2,768	2,098

Non-current assets

Property, plant and equipment	8	14,554	11,417
Intangible assets	9	30	76
Long-term investments	10	332	34
Other long-term assets	11	233	274

Total assets 17,917 13,899

Regulatory deferrals 12 117 164

Total assets and regulatory deferrals 18,034 14,063

LIABILITIES AND EQUITY

Current liabilities

Short-term borrowings	14	369	435
Trade and other payables	13	584	1,162
Current portion of long-term debt	14	7	143
Derivative liabilities		8	5
Current portion of other liabilities	16, 17, 18	2	5

Total current liabilities 970 1,750

Non-current liabilities

Long-term debt	14	9,386	5,873
Class B limited partnership units	15	491	399
Deferred credits	16	1,752	1,161
Deferred contributions	17	11	11
Decommissioning liabilities	18	86	82
Long-term payables	19	52	58
Employee future benefits	20	126	117

Total liabilities 12,874 9,451

Shareholder's equity

Share capital	21	123	123
Shareholder contributions	21	3,693	2,861
Reserves		(71)	7
Retained earnings		1,336	1,273

Total equity 5,081 4,264

Total liabilities and equity 17,955 13,715

Regulatory deferrals 12 79 348

Total liabilities, equity and regulatory deferrals 18,034 14,063

Commitments and contingencies (Note 32)

Subsequent event (Note 35)

See accompanying notes

On behalf of the Board:

DIRECTOR

DIRECTOR

NALCOR ENERGY
CONSOLIDATED STATEMENT OF PROFIT AND COMPREHENSIVE (LOSS) INCOME

<i>For the year ended December 31 (millions of Canadian dollars)</i>	Notes	2017	2016
Energy sales	23	858	779
Other revenue	23	72	45
Revenue		930	824
Fuels		226	168
Power purchased		62	61
Operating costs	24	219	207
Production, marketing and transportation costs	25	36	26
Transmission rental and market fees	26	25	22
Depreciation, depletion, amortization and impairment	8,9	300	135
Exploration and evaluation		1	2
Net finance expense	27	66	72
Other expense (income)	28	23	(4)
Expenses		958	689
(Loss) profit before regulatory adjustments		(28)	135
Regulatory adjustments	12	(91)	(1)
Profit for the year		63	136
Other comprehensive loss			
Total items that may or have been reclassified to profit or loss:			
Actuarial loss on employee future benefits	20,29	(3)	-
Net fair value (loss) gain on available-for-sale financial instruments	29	(2)	13
Net fair value loss on cash flow hedges	29	(66)	(2)
Reclassification adjustments related to:			
Available-for-sale financial instruments	29	(8)	(10)
Cash flow hedges recognized in profit or loss	29	1	(6)
Other comprehensive loss for the year		(78)	(5)
Total comprehensive (loss) income for the year		(15)	131

See accompanying notes

NALCOR ENERGY
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

<i>(millions of Canadian dollars)</i>	Notes	Share Capital	Shareholder Contributions	Fair Value Reserve	Employee Benefit Reserve	Retained Earnings	Total
Balance at January 1, 2017		123	2,861	34	(27)	1,273	4,264
Profit for the year		-	-	-	-	63	63
Other comprehensive (loss) income							
Net change in fair value of available-for-sale financial instruments	29	-	-	(2)	-	-	(2)
Net change in fair value of cash flow hedges	29	-	-	(66)	-	-	(66)
Net change in fair value of financial instruments reclassified to profit or loss	29	-	-	(7)	-	-	(7)
Actuarial loss on employee future benefits	20,29	-	-	-	(3)	-	(3)
Total comprehensive (loss) income for the year		-	-	(75)	(3)	63	(15)
Shareholder contributions	21	-	832	-	-	-	832
Balance at December 31, 2017		123	3,693	(41)	(30)	1,336	5,081
Balance at January 1, 2016		123	2,204	39	(27)	1,137	3,476
Profit for the year		-	-	-	-	136	136
Other comprehensive (loss) income							
Net change in fair value of available-for-sale financial instruments	29	-	-	13	-	-	13
Net change in fair value of cash flow hedges	29	-	-	(2)	-	-	(2)
Net change in fair value of financial instruments reclassified to profit or loss	29	-	-	(16)	-	-	(16)
Total comprehensive (loss) income for the year		-	-	(5)	-	136	131
Shareholder contributions	21	-	657	-	-	-	657
Balance at December 31, 2016		123	2,861	34	(27)	1,273	4,264

See accompanying notes

NALCOR ENERGY

CONSOLIDATED STATEMENT OF CASH FLOWS

<i>For the year ended December 31 (millions of Canadian dollars)</i>	Notes	2017	2016
Operating activities			
Profit for the year		63	136
Adjusted for the following non-cash items:			
Depreciation, depletion and impairment - property, plant and equipment	8	203	125
Amortization and impairment - intangible assets	9	97	10
Accretion	27	7	7
Loss on disposal of property, plant and equipment	28	20	7
Sinking fund earnings		(13)	(15)
Regulatory adjustments	12	(91)	(1)
Other		5	(4)
		291	265
Changes in non-cash working capital balances	33	(81)	(46)
Net cash provided from operating activities		210	219
Investing activities			
Additions to property, plant and equipment	34	(2,748)	(2,741)
Additions to intangible assets	9,34	(51)	(36)
Change in long-term receivables	11	28	(24)
Change in sinking fund		90	(6)
Withdrawal from reserve fund	11	15	16
Change in short-term investments		(961)	935
Change in long-term investments		(298)	57
Proceeds on disposal of property, plant and equipment		12	1
Other		(1)	(2)
Changes in non-cash working capital balances	33	(623)	177
Net cash used in investing activities		(4,537)	(1,623)
Financing activities			
Proceeds from long-term debt	14	3,516	-
Retirement of long-term debt	14	(150)	(225)
Change in restricted cash		341	458
Class B limited partnership unit contributions	15	55	168
Change in short-term borrowings		(66)	338
Change in shareholder contributions	21	832	657
Rate stabilization plan payout	12	(131)	-
Settlement of cash flow hedges		(67)	-
Other		(3)	2
Net cash provided from financing activities		4,327	1,398
Net increase (decrease) in cash and cash equivalents		-	(6)
Cash and cash equivalents, beginning of year		143	149
Cash and cash equivalents, end of year		143	143
Interest received		51	27
Interest paid		317	277

See accompanying notes

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS

Nalcor Energy (Nalcor or the Company) is incorporated under a special act of the Legislature of the Province of Newfoundland and Labrador (the Province) as a Crown corporation and its business includes the development, generation, transmission and sale of electricity, oil and gas, industrial fabrication and energy marketing. Nalcor's head office is located at 500 Columbus Drive in St. John's, Newfoundland and Labrador A1B 0C9, Canada.

1.1 Subsidiaries

Nalcor holds interests in the following subsidiaries:

A 100% interest in Newfoundland and Labrador Hydro (Hydro), whose principal activity is the generation, transmission and sale of electricity. Hydro's operations include both regulated and non-regulated activities.

A 100% interest in Nalcor Energy – Oil and Gas Inc. (Oil and Gas). Oil and Gas has a mandate to engage in the upstream and downstream sectors of the oil and gas industry. Upstream includes exploration, development, and production activities, while downstream includes transportation and processing activities.

A 100% interest in Nalcor Energy – Bull Arm Fabrication Inc. (Bull Arm Fabrication), an industrial fabrication site with a fully integrated infrastructure to support large-scale fabrication and assembly. Its facilities include onshore fabrication halls and shops, a dry-dock and a deep water site.

A 100% interest in Nalcor Energy Marketing Corporation (Energy Marketing), a subsidiary established to market Nalcor's energy throughout North America.

A 100% interest in Muskrat Falls Corporation (Muskrat Falls), created to develop, construct, finance and operate the Muskrat Falls plant, an 824 megawatt (MW) hydroelectric generating facility in Labrador.

A 100% interest in Labrador Transmission Corporation (Labrador Transco), created to develop, construct, finance and operate transmission assets connecting the Muskrat Falls plant to the existing hydroelectric generating facility in Churchill Falls.

A 100% interest in Labrador-Island Link General Partner Corporation (LIL GP) and Labrador-Island Link Holding Corporation (LIL Holdco), created to control, manage and hold Nalcor's interest in the Labrador-Island Link Limited Partnership (LIL LP).

A 100% interest in Labrador-Island Link Operating Corporation (LIL Opco), created to operate and maintain the Labrador-Island Link (LIL).

A 100% interest in Lower Churchill Management Corporation (LCMC), created to carry out the project development and management functions for Phase 1 of the Lower Churchill Project (LCP) including planning, engineering and design management, construction management, risk management, finance, procurement and supply chain management.

A limited partnership interest in the LIL LP, created to develop, construct, finance and operate the assets and property constituting the LIL, a transmission link to be constructed between the Muskrat Falls plant and the Newfoundland and Labrador Island Interconnected System. LIL Holdco holds 100% of the Class A and Class C limited partnership units.

Nalcor also holds a 100% interest in Gull Island Power Company Limited (GIPCo) and, through Hydro, a 51.0% interest in Lower Churchill Development Corporation Limited (LCDC), both of which are inactive.

1.2 Investment in Joint Arrangement

Nalcor holds a 65.8% beneficial interest (through Hydro) in Churchill Falls (Labrador) Corporation Limited (Churchill Falls), a joint operation that owns and operates a hydroelectric generating plant and related transmission facilities situated in Labrador with a rated capacity of 5,428 MW.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Nalcor holds a 33.33% beneficial interest (through Churchill Falls) in Twin Falls Power Corporation Limited (Twin Falls).

1.3 Structured Entities

Nalcor consolidates the results of structured entities in which it holds a financial interest and is the primary beneficiary. Nalcor has determined that it is the primary beneficiary of the LIL Construction Project Trust (the IT) and, as a result, has included the financial statements of the IT in these annual audited consolidated financial statements. Nalcor has determined that it is not the primary beneficiary of the Muskrat Falls/Labrador Transmission Assets (MF/LTA) Funding Trust or the LIL Funding Trust and therefore the operations of these trusts are not reflected in these annual audited consolidated financial statements.

2. SIGNIFICANT ACCOUNTING POLICIES

2.1 Statement of Compliance and Basis of Measurement

These annual audited consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB). Nalcor has adopted accounting policies which are based on the IFRS applicable as at December 31, 2017 and includes individual IFRS, International Accounting Standards (IAS), and interpretations made by the IFRS Interpretations Committee and the Standing Interpretations Committee.

These annual audited consolidated financial statements have been prepared on a historical cost basis, except for financial instruments at fair value through profit or loss (FVTPL) and available-for-sale (AFS) which have been measured at fair value. The annual audited consolidated financial statements are presented in Canadian Dollars (CAD) and all values rounded to the nearest million, except when otherwise noted. The annual audited consolidated financial statements were approved by Nalcor's Board of Directors (the Board) on March 2, 2018.

2.2 Basis of Consolidation

The annual audited consolidated financial statements include the financial statements of Nalcor, its subsidiary companies and its share of investments in joint arrangements. In addition, the financial statements of all structured entities, for which Nalcor has been determined the primary beneficiary, are included in these annual audited consolidated financial statements. Intercompany transactions and balances have been eliminated upon consolidation.

Effective June 18, 1999, Hydro, Churchill Falls, and Hydro-Québec entered into a shareholders' agreement (the Shareholders' Agreement) which provided, among other matters, that certain of the strategic operating, financing and investing policies of Churchill Falls be subject to approval jointly by representatives of Hydro and Hydro-Québec on Churchill Falls' Board of Directors. Although Hydro holds a 65.8% ownership interest, the agreement changed the nature of the relationship between Hydro and Hydro-Québec, with respect to Churchill Falls, from that of majority and minority shareholders, respectively, to that of a joint operation. Accordingly, Hydro has recognized its share of assets, liabilities and profit or loss in relation to its interest in Churchill Falls subsequent to the effective date of the Shareholders' Agreement.

Churchill Falls' investment in Twin Falls is accounted for using the equity method.

Substantially all of Oil and Gas' activities are conducted jointly with others and, accordingly, these annual audited consolidated financial statements reflect only Nalcor's proportionate interest in such activities.

2.3 Cash and Cash Equivalents and Short-term Investments

Cash and cash equivalents consist of amounts on deposit with Schedule 1 Canadian Chartered banks, as well as highly liquid investments with maturities of three months or less. Investments with maturities greater than three months and less than twelve months are classified as short-term investments. Cash and cash equivalents are measured at cost which approximates fair value, while short-term investments are measured at fair value.

2.4 Restricted Cash

Restricted cash consists of cash held on deposit with Schedule 1 Canadian Chartered banks and administered by the Collateral

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Agent for the sole purpose of funding construction costs related to the LIL, Labrador Transmission Assets (LTA) and Muskrat Falls' hydroelectric plant, including pre-funded equity requirements required under the Labrador-Island Link Limited 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 MF/LTA PFA. Restricted cash also includes accounts administered by the Trustee of the IT which are associated with the establishment of the IT. Restricted cash is measured at cost which approximates fair value.

2.5 Trade and Other Receivables

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

2.6 Inventories

Inventories are carried at the lower of cost and net realizable value. Cost is determined on a weighted average basis and includes expenditures incurred in acquiring the inventories and bringing them to their existing condition and location. Net realizable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale.

2.7 Property, Plant and Equipment

Items of property, plant and equipment are recognized using the cost model and thus are recorded at cost less accumulated depreciation and accumulated impairment losses. Cost includes materials, labour, contracted services, professional fees and, for qualifying assets, borrowing costs capitalized in accordance with Nalcor's accounting policy outlined in Note 2.11. Costs capitalized with the related asset include all those costs directly attributable to bringing the asset into operation. When significant parts of property, plant and equipment are required to be replaced at intervals, Nalcor 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. Property, plant and equipment is not revalued for financial reporting purposes. Depreciation of these assets commences when the assets are ready for their intended use.

Hydro

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

Generation plant	
Hydroelectric	45 to 100 years
Thermal	35 to 65 years
Diesel	25 to 55 years
Transmission	
Lines	30 to 65 years
Terminal stations	40 to 55 years
Distribution system	30 to 55 years
Other assets	5 to 55 years

Hydroelectric generation plant includes the powerhouse, turbines, governors and generators, as well as water conveying and control structures, including dams, dikes, tailrace, penstock and intake structures. Thermal generation plant is comprised of the powerhouse, turbines and generators, boilers, oil storage tanks, stacks, and auxiliary systems. Diesel generation plant includes the buildings, engines, generators, switchgear, fuel storage and transfer systems, dikes and liners and cooling systems.

Transmission lines include the support structures, foundations and insulators associated with lines at voltages of 230, 138 and 69 kilovolt (kV). Terminal stations assets are used to step up voltages of electricity and to step down voltages for distribution. Distribution system assets include poles, transformers, insulators, and conductors.

Other assets include telecontrol, buildings, vehicles, furniture, tools and equipment.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Churchill Falls

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

Hydroelectric generation plant	25 to 100 years
Transmission and terminals	30 to 65 years
Service facilities and other	5 to 45 years

Hydro and Churchill Falls assets' residual values, useful lives and method of depreciation are reviewed at each financial year end and adjusted prospectively, if appropriate. The carrying value of property, plant and equipment is reviewed for impairment whenever events indicate that the carrying amounts of those assets may not be recoverable.

Oil and Gas

(i) Development and Production Costs

Items of property, plant and equipment, which include petroleum and natural gas development and production assets, are carried at cost less accumulated depreciation, depletion and impairment. Development and production assets are grouped into cash-generating units (CGUs) for impairment testing.

Expenditures on the construction, installation or completion of infrastructure facilities such as processing facilities and the drilling of development wells, including unsuccessful development or delineation wells, are capitalized within property, plant and equipment, as long as it is technically feasible and economically viable to extract identified reserves.

The initial cost of an asset comprises its purchase price or construction cost, any costs directly attributable to bringing the asset into operation, the initial estimate of the decommissioning costs and, for qualifying assets, borrowing costs. The purchase price or constructed cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset.

Capitalized petroleum and natural gas interests generally represent costs incurred in developing proved and/or probable reserves and bringing in or enhancing production from such reserves, and are accumulated on a field or geotechnical area basis.

Gains and losses on disposal of an item of property, plant and equipment, including petroleum and natural gas interests, are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment and are recorded in other expense (income).

(ii) Subsequent Costs

Costs incurred subsequent to the determination of technical feasibility and commercial viability are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the asset will flow to Oil and Gas and the cost can be measured reliably. The carrying amount of a replaced asset is derecognized when replaced. Routine repair and maintenance costs are charged to profit or loss during the period in which they are incurred.

(iii) Depletion

The net carrying value of development and production assets is depleted using the unit of production method by reference to the ratio of production in the year to the related proved and probable reserves, and considering estimated future development costs necessary to bring those reserves into production. Future development costs are estimated taking into account the level of development required to produce the reserves. These estimates are reviewed by independent reserve engineers at least annually.

Proved and probable reserves are estimated using independent reserve engineer reports and represent the estimated quantities of crude oil, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate,

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

with a specified degree of certainty, to be recoverable in future years from known reservoirs and which are considered commercially viable. It is equally likely that the actual remaining quantities recovered will be greater or less than the sum of the estimated proved plus probable reserves.

Such reserves may be considered commercially producible if management has the intention of developing and producing them and such intention is based upon:

- a reasonable assessment of the future economics of such production;
- a reasonable expectation that there is a market for all (or substantially all) of the expected petroleum and natural gas production; and
- evidence that the necessary production, transshipment and transportation facilities are available or can be made available.

Other Assets

Office equipment and computer hardware are carried at cost less accumulated depreciation. Depreciation is recognized in profit or loss on a straight-line basis over the estimated useful life of 5 to 20 years. Depreciation methods, useful lives and residual values are reviewed at each reporting date.

Lower Churchill Project

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

Project support assets	4 to 7 years
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As use of the project support assets are directly attributable to the construction of the Muskrat Falls hydroelectric plant and LTA, related depreciation costs are capitalized as incurred, until such time as the assets are substantially ready for their intended use or sale.

2.8 Exploration and Evaluation Assets

Pre-license exploration and evaluation costs are recognized in profit or loss as incurred. Costs of exploring for and evaluating licensed petroleum and gas properties are capitalized and the resulting intangible exploration and evaluation assets are tested for impairment in accordance with IFRS 6 and IAS 36.

Exploration and evaluation costs related to each license/prospect are initially capitalized with "Exploration and Evaluation Assets." Such exploration and evaluation costs may include costs of license acquisition, technical services and studies, exploration drilling and testing, directly attributable overhead and administrative expenses and the projected costs of retiring the assets. General prospecting or evaluation costs incurred prior to having obtained the legal rights to explore an area are expensed directly to profit or loss as they are incurred.

Exploration and evaluation assets are not depleted and are carried forward until technical feasibility and commercial viability of extracting a mineral resource is considered to be determined. The technical feasibility and commercial viability of extracting a mineral resource is considered to be determined when proved reserves are determined to exist. A review of each exploration license or field is carried out, at least annually, to ascertain whether proved reserves have been discovered.

Upon determination of proved reserves, exploration and evaluation assets attributable to those reserves are first tested for impairment and then reclassified from exploration and evaluation assets to property, plant and equipment.

2.9 Investment Property

Investment property is property held for the purpose of generating rental income or capital appreciation, but not for sale in the ordinary course of business, use in the production or supply of goods or services or for administrative purposes. As at December 31, 2017, investment property includes the Bull Arm Fabrication site and facilities.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Investment property is recognized using the cost model and thus is recorded at cost less accumulated depreciation and accumulated impairment losses. Cost includes materials, labour, contracted services and professional fees. Costs capitalized with the related asset include all those costs directly attributable to bringing the asset into operation. When significant parts of investment property are required to be replaced at intervals, Nalcor recognizes such parts as individual assets with specific useful lives and depreciation, respectively. Likewise, when a major inspection is performed, its cost is recognized in the carrying amount of the investment property as a replacement if the recognition criteria are satisfied. All other repair and maintenance costs are recognized in the Consolidated Statement of Profit and Comprehensive (Loss) Income as incurred. Investment property is not revalued for financial reporting purposes. Depreciation of these assets commences when the assets are ready for their intended use.

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

Computer equipment, vehicles and office equipment	5 years
Buildings	18 years
Topsides module hall door	26 years
Visitor center	42 years

The assets' residual values, useful lives and method of depreciation are reviewed at each fiscal year end and adjusted prospectively, if appropriate. The carrying value of investment property is reviewed for impairment whenever events indicate that the carrying amounts of those assets may not be recoverable.

2.10 Intangible Assets

Intangible assets that are expected to generate future economic benefit and are measurable, including computer software costs, costs of technical services, feasibility studies, exploration assets and intellectual property are capitalized as intangible assets in accordance with IAS 38.

Intangible assets with finite useful lives are carried at cost less accumulated amortization and accumulated impairment losses. The estimated useful life and amortization method are reviewed at the end of each 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.

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

Computer software	5 to 10 years
Feasibility studies	5 to 20 years
Seismic data acquisitions	6 years

2.11 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 Consolidated Statement of Profit and Comprehensive (Loss) Income in the period in which they are incurred.

2.12 Impairment of Non-Financial Assets

At the end of each reporting period, Nalcor reviews the carrying amounts of its non-financial assets, except for exploration and evaluation assets, to determine whether there is any indication that those assets may be impaired. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. Exploration and evaluation assets are assessed for impairment when they are reclassified to plant, property and equipment and also if there are indicators that suggest that the carrying amount exceeds the recoverable amount.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Where it is not possible to estimate the recoverable amount of an individual asset, Nalcor estimates the recoverable amount of the CGU to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual CGUs, or otherwise they are allocated to the smallest group of CGUs for which a reasonable and consistent allocation basis can be identified. The recoverable amount is the higher of fair value less costs of disposal 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.

Exploration and evaluation assets are allocated to the CGUs on a project basis when they are assessed for impairment, both at the time of any triggering facts and circumstances as well as upon their reclassification to property, plant and equipment.

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 Consolidated Statement of Profit and Comprehensive (Loss) Income.

2.13 Investments in Joint Arrangements

A joint arrangement is an arrangement of which two or more parties involved have joint control. Control exists when Nalcor has the power, directly or indirectly, to govern the financial and operating policies of another entity, so as to obtain benefits from its activities. A joint arrangement is either classified as a joint operation or a joint venture based on the rights of the parties involved.

Nalcor holds equity stakes in the Hebron, Hibernia South Extension and White Rose Extension projects. These projects are classified as joint operations as multiple parties hold joint control and stakeholders have rights to the project assets and obligations for its liabilities. Nalcor accounts for its oil and gas investments by recognizing its share of assets, liabilities and profit or loss in relation to its interest in the joint operation.

Effective June 18, 1999, Hydro, Churchill Falls and Hydro-Québec entered into the Shareholders' Agreement which provided, among other matters, that certain of the strategic operating, financing and investing policies of Churchill Falls be subject to approval jointly by representatives of Hydro and Hydro-Québec on the Board of Directors of Churchill Falls. Although Nalcor (through Hydro) retains its 65.8% ownership interest, the agreement changed the nature of the relationship between Hydro and Hydro-Québec, with respect to Churchill Falls, from that of majority and minority shareholders, respectively, to that of joint operators. This investment is accounted for using the proportionate consolidation method.

Hydro's joint operation, Churchill Falls, holds 33.33% of the equity share capital of Twin Falls and is a party with other shareholders in a participation agreement which gives Churchill Falls joint control of Twin Falls. This investment is accounted for using the equity method. Under the equity method, the interest in the joint venture is carried in the Statement of Financial Position at cost plus post acquisition changes in Churchill Falls' share of net assets of the joint venture. The Consolidated Statement of Profit and Comprehensive (Loss) Income reflects the share of the profit or loss of the joint venture.

2.14 Employee Future Benefits

(i) Pension Plan

Employees participate in the Province's Public Service Pension Plan, a multi-employer defined benefit plan. Contributions by Nalcor to this Plan are recognized as an expense when employees have rendered service entitling them to the contributions. Liabilities associated with this Plan are held with the Province.

(ii) Other Benefits

Nalcor provides group life insurance and health care benefits on a cost-shared basis to retired employees, in addition to a retirement allowance.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

The cost of providing these benefits is determined using the projected unit credit method, with actuarial valuations being completed on an annual basis, based on service and Management's best estimate of salary escalation, retirement ages of employees and expected health care costs.

Actuarial gains and losses on Nalcor's defined benefit obligation are recognized in reserves in the period in which they occur. Past service costs are recognized in operating costs as incurred. Pursuant to Order No. P.U. 36 (2015), Nalcor recognizes the amortization of Hydro's employee future benefit actuarial gains and losses in the Consolidated Statement of Profit and Comprehensive (Loss) Income as a regulatory adjustment.

The retirement benefit obligation recognized in the Consolidated Statement of Financial Position represents the present value of the defined benefit obligation.

2.15 Provisions

A provision is a liability of uncertain timing or amount. A provision is recognized if Nalcor 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 Consolidated Statement of Financial Position date using the current discount rate.

2.16 Decommissioning, Restoration and Environmental Liabilities

Legal and constructive obligations associated with the retirement of property, plant and equipment are recorded as liabilities when those obligations are incurred and are measured as the present value of the expected costs to settle the liability, discounted at a rate specific to the liability. The liability is accreted up to the date the liability will be incurred with a corresponding charge to net finance expense. The carrying amount of decommissioning, restoration and environmental liabilities is reviewed annually with changes in the estimates of timing or amount of cash flows added to or deducted from the cost of the related asset or expensed in the Consolidated Statement of Profit and Comprehensive (Loss) Income if the liability is short-term in nature.

2.17 Revenue Recognition

Electricity Sales

Revenue from the sale of energy is recognized when Nalcor has transferred the significant risks and rewards of ownership to the buyer, recovery of the consideration is probable and the amount of revenue can be reliably measured. Sales within the Province are primarily at rates approved by the Newfoundland and Labrador Board of Commissioners of Public Utilities (PUB), whereas export sales and sales to certain major industrial customers are either at rates under the terms of the applicable contracts, or at market rates.

Churchill Falls provides energy to two primary customers: Hydro-Québec and Hydro.

A power contract with Hydro-Québec dated May 12, 1969 (the Power Contract) provides for the sale of a significant amount of the energy from Churchill Falls. The Power Contract had a 40-year term that expired August 31, 2016, and was followed by a Renewed Power Contract with Hydro-Québec for an additional 25 years beginning September 1, 2016. The rate was predetermined in the Power Contract and was 2.5426 mills per kWh. The rate during the term of the Renewed Power Contract is 2.0 mills per kWh.

Churchill Falls also recognizes revenue from Hydro-Québec under a Guaranteed Winter Availability Contract (GWAC) through 2041. The GWAC was signed with Hydro-Québec in 1998 and provides for the sale of 682 MW of guaranteed seasonal availability to Hydro-Québec during the months of November through March in each of the remaining years until 2041.

Under the Power Contract and Renewed Power Contract, Churchill Falls has the right to recall 300 MW (Recall Power). All of the

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Recall Power is sold by Churchill Falls to Hydro. Churchill Falls also provides an additional 225 MW to Hydro.

Petroleum and Natural Gas Sales

Revenue from the sale of crude oil is recognized when the amount of revenue can be reasonably measured, the significant risks and rewards of ownership have passed to the buyer and collection is reasonably assured. This typically occurs when the oil has been produced and delivered to the transshipment facility.

Revenue from properties in which Nalcor has an interest with other producers is recognized on the basis of Nalcor's net working interest of petroleum and natural gas produced (the entitlement method). Under this method, crude oil produced below or above Nalcor's net working interest results in an under-lift or over-lift position. Under-lift or over-lift positions are measured at market value and recorded as an asset or liability, respectively.

Other Revenue

Revenue associated with the sale of geoscience data is recognized when the terms and conditions governing sales have been met, the amount of revenue can be reliably measured and recovery of the consideration is probable.

2.18 Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Lessor accounting

Amounts due from lessees under finance leases are recognized as receivables at the amount of Nalcor's net investment in the leases. Finance lease income is allocated to accounting periods so as to reflect a constant periodic rate of return on Nalcor's net investment outstanding in respect of the leases.

Rental income from operating leases is recognized on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognized on a straight-line basis over the lease term.

Lessee accounting

Assets held under finance leases are initially recognized as assets of Nalcor at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the Consolidated Statement of Financial Position as a finance lease obligation.

Lease payments are apportioned between finance expenses and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance expenses are recognized immediately in profit or loss, unless they are directly attributable to qualifying assets, in which case they are capitalized in accordance with Nalcor's general policy on borrowing costs (Note 2.11). Contingent rental costs are recognized as operating costs in the periods in which they are incurred.

Operating lease payments are recognized as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognized as an expense in the period in which they are incurred.

In the event that lease incentives are received to enter into operating leases, such incentives are recognized as a liability. The aggregate benefit of incentives is recognized as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

2.19 Foreign Currencies

Transactions in currencies other than Nalcor'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

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

items denominated in foreign currencies are translated at the rates of exchange in effect at the period end date. Foreign exchange gains and losses not included in regulatory deferrals are recorded in the Consolidated Statement of Profit and Comprehensive (Loss) Income as other expense (income).

2.20 Income Taxes

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

2.21 Financial Instruments

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

Classification of Financial Instruments

Nalcor has classified each of its financial instruments into the following categories: financial assets at FVTPL, loans and receivables, held-to-maturity investments, AFS financial assets, financial liabilities at FVTPL, financial instruments used for hedging and other financial liabilities.

<u>Financial instrument</u>	<u>Category</u>
Cash and cash equivalents	Loans and receivables
Restricted cash	Loans and receivables
Short-term investments	AFS financial assets
Trade and other receivables	Loans and receivables
Derivative instruments	At FVTPL and financial instruments used for hedging
Sinking funds – investments in same Hydro issue	Held-to-maturity investments
Sinking funds – other investments	AFS financial assets
Reserve fund	AFS financial assets
Long-term receivables	Loans and receivables
Long-term investments (including current portion)	Held-to-maturity investments
Trade and other payables	Other financial liabilities
Short-term borrowings	Other financial liabilities
Long-term debt	Other financial liabilities
Long-term payables	Other financial liabilities
Class B limited partnership units	Other financial liabilities

(i) Effective Interest Method

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

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

Financial Assets

(ii) Financial Assets at FVTPL

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

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling it in the near term; or
- on initial recognition it is part of a portfolio of identified financial instruments that Nalcor manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

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

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial asset forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with Nalcor's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 Financial Instruments: Recognition and Measurement permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial assets at FVTPL are stated at fair value, with any gains or losses arising on re-measurement recognized in other expense (income). The net gain or loss incorporates any dividends or interest earned.

(iii) Loans and Receivables

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

(iv) Held-to-Maturity Investments

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

(v) AFS Financial Assets

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

Financial Liabilities and Equity Instruments

(vi) Financial Liabilities at FVTPL

A financial liability may be classified as at FVTPL if the contracted liability contains one or more embedded derivatives, and if the embedded derivative significantly modified the cash flows or if the embedded derivative is not closely related to the host liability. Financial liabilities at FVTPL are stated at fair value, with any gains or losses arising from re-measurement recognized in profit or loss.

(vii) Other Financial Liabilities

Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs. Other financial

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

liabilities are subsequently measured at amortized cost using the effective interest method, with interest expense recognized on an effective yield basis.

(viii) Derivative Instruments and Financial Instruments Used for Hedging

Derivative instruments are utilized by Nalcor to manage risk. Nalcor's policy is not to utilize derivative instruments for speculative purposes. Derivatives are initially measured at fair value at the date the derivative contracts are entered into and are subsequently measured at their fair value at the end of each reporting period. The resulting gain or loss is recognized in profit or loss immediately unless the derivative is designated and effective as a hedging relationship.

Nalcor may choose to designate derivative instruments as hedges and apply hedge accounting if there is a high degree of correlation between the price movements in the derivative instruments and the hedged items. Nalcor 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.

Hedges which meet the strict criteria for hedge accounting are accounted for as follows:

Cash Flow Hedges

The effective portion of the gain or loss on the hedging instrument is recognized directly in other comprehensive loss, while any ineffective portion is recognized immediately in the Consolidated Statement of Profit and Comprehensive (Loss) Income for the year.

Amounts recognized in other comprehensive loss are transferred to the Consolidated Statement of 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.

2.22 **Derecognition of Financial Instruments**

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

2.23 **Impairment of Financial Assets**

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

Evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- the borrower, more probable than not, entering into bankruptcy or financial re-organization.

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

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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

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

When an AFS financial asset is considered to be impaired, cumulative gains or losses previously recognized in other comprehensive loss are reclassified to profit or loss in the period.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized.

2.24 Government Grants

Government grants are recognized when there is reasonable assurance that Nalcor will comply with the associated conditions and that the grants will be received.

Government grants are recognized in profit or loss on a systematic basis over the periods in which Nalcor recognizes as expenses the related costs for which the grants are intended to compensate. Specifically, government grants whose primary condition is that Nalcor should purchase, construct or otherwise acquire non-current assets are recognized as deferred revenue in the Consolidated Statement of Financial Position and transferred to the Consolidated Statement of Profit and Comprehensive (Loss) Income on a systematic and rational basis over the useful lives of the related assets.

Government grants that are receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to Nalcor with no future related costs are recognized in the Consolidated Statement of Profit and Comprehensive (Loss) Income in the period in which they become receivable.

2.25 Regulatory Deferrals

Hydro's revenues from its electrical sales to most customers within the Province are subject to rate regulation by the PUB. Hydro's borrowing and capital expenditure programs are also subject to review and approval by the PUB. Rates are set through periodic general rate applications utilizing a cost of service methodology. The preliminary estimate of Hydro's allowed rate of return based upon Board Order No. P.U. 49 (2016) is 6.6% in 2017 and 6.6% in 2016 +/- 20 basis points. Hydro applies various accounting policies that differ from enterprises that do not operate in a rate regulated environment. Generally, these policies result in the deferral and amortization of costs or credits which are expected to be recovered or refunded in future rates. In the absence of rate regulation, these amounts would be included in the determination of profit or loss in the year the amounts are incurred. The effects of rate regulation on the annual audited consolidated financial statements are disclosed in Note 12.

3. SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUMPTIONS

The preparation of the annual audited consolidated 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. Actual results may differ materially from these estimates, including changes as a result of future decisions made by the PUB. 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.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

3.1 Use of Judgments

(i) Asset Impairment and Reversals

Nalcor applies judgment in evaluating impairment and impairment reversal indicators based on various internal and external factors.

The recoverable amount of a CGU or asset is determined based on the higher of fair value less costs of disposal and its value in use. Management uses factors including expected future oil prices and proved and probable reserves from third party specialists and discount rates to determine the recoverable amount, as well as judgments regarding the occurrence of future events. Changes in these factors will affect the recoverable amount of CGUs and assets, which may result in a material adjustment to their carrying value.

(ii) Property, Plant and Equipment

Nalcor's accounting policy relating to property, plant and equipment is described in Note 2.7. 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 Nalcor's property, plant and equipment.

(iii) Revenue

Management exercises judgment in estimating the value of electricity consumed by retail customers in the period, but billed subsequent to the end of the reporting period. Specifically, this involves an estimate of consumption for each retail customer, based on the customer's past consumption history.

When recognizing deferrals and related amortization of costs or credits in Hydro Regulated, Management assumes that such costs or credits will be recovered or refunded through customer rates in future years. Recovery of some of these deferrals is subject to a future PUB order. As such, there is a risk that some or all of the regulatory deferrals will not be approved by the PUB which could have a material impact on Hydro Regulated's profit or loss in the year the order is received.

(iv) Functional Currency

Functional currency was determined by evaluating the primary economic environment in which Nalcor operates. As Nalcor 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 Canadian Dollars.

(v) Determination of CGUs

Nalcor's accounting policy relating to impairment of non-financial assets is described in Note 2.12. In applying this policy, Nalcor groups assets into the smallest identifiable groups for which cash flows are largely independent of the cash flows from other assets or groups of assets. Judgment is used in determining the level at which cash flows are largely independent of other assets or groups of assets.

(vi) Discount Rates

Certain of Nalcor's financial liabilities are discounted using discount rates that are subject to Management's judgment.

(vii) Consolidation of Joint Arrangements

Management exercises judgment when applying the criteria outlined in IFRS 11 to determine whether joint arrangements constitute joint ventures or joint operations. Management has determined that its interest in Churchill Falls is considered a joint operation and its interest in Twin Falls is considered a joint venture.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(viii) Consolidation

Management applies its judgment when determining whether to consolidate structured entities in accordance with the criteria outlined in IFRS 10. Management has determined that the Company should consolidate the IT but should not consolidate the MF/LTA and LIL Funding Trusts.

3.2 Use of Estimates

(i) Property, Plant and Equipment

Amounts recorded for depreciation are based on the useful lives of Nalcor's assets. The useful lives of property, plant and equipment are determined by independent specialists and reviewed annually by Nalcor. These useful lives are Management's best estimate of the service lives of these assets. Changes to these lives could materially affect the amount of depreciation recorded.

(ii) Investment Property

Due to the nature of the property and lack of comparable market data, the fair value of Nalcor's investment property is determined using the present value of the 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.

(iii) Intangible Assets

Amounts recorded for amortization are based on the useful lives of Nalcor's assets. These useful lives are Management's best estimate of the service lives of these assets. Changes to these lives could materially affect the amount of amortization recorded.

(iv) Oil and Natural Gas Reserves

Oil and natural gas reserves are evaluated by independent reserve engineers. Reserve estimates are used in calculating depletion, impairment and decommissioning liabilities. Estimates of recoverable reserves are based upon variable factors and assumptions regarding historical production, production rates, ultimate reserve recovery, marketability of petroleum and natural gas, and timing and amount of future cash expenditures. Changes to these amounts could materially affect these calculations.

(v) Partnership Unit Liabilities

LIL LP determines the fair value of the Class B limited partnership units at each financial reporting date. These units represent the limited partners' ownership interests in the Partnership. Due to the nature of the liabilities and lack of comparable market data, the fair value of these units 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 financial liabilities 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.

(vi) Decommissioning Liabilities

Nalcor recognizes a liability for the fair value of the future expenditures required to settle obligations associated with the retirement of property, plant and equipment. Decommissioning liabilities are recorded as a liability at fair value, with a corresponding increase to property, plant and equipment. Accretion of decommissioning liabilities is included in the Consolidated Statement of Profit and Comprehensive (Loss) Income through net finance expense. Differences between the recorded decommissioning liabilities and the actual decommissioning costs incurred are recorded as a gain or loss in the settlement period.

(vii) Employee Future Benefits

Nalcor provides group life insurance and health care benefits on a cost-shared basis to retired employees, in addition to a

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

severance payment upon retirement. The expected cost of providing these other employee benefits is accounted for on an accrual basis, and has been actuarially determined using the projected unit credit method prorated on service, and Management's best estimate of salary escalation, retirement ages of employees, and expected health care costs.

(viii) Revenue

In the absence of a signed agreement with Hydro-Québec relating to the Annual Energy Base (AEB), Churchill Falls has an agreement with Hydro-Québec to continue to use the 2008 AEB on an interim basis until final judgment is obtained in the Declaratory Judgment case.

3.3 Use of Assumptions

(i) Derivative Assets

Fair value assumptions for financial transmission rights have been based on internal valuation techniques and models that extrapolate observable external market inputs, such as commodity prices, and include significant judgment regarding the expected impact of seasonality and locational adjustments.

4. CURRENT AND FUTURE CHANGES IN ACCOUNTING POLICIES

IAS 7 - Disclosure Initiative became effective for accounting periods commencing on January 1, 2017 and did not have a material impact on Nalcor's annual audited consolidated financial statements.

The amendments require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. The amendments do not prescribe a specific format to disclose financing activities; however, an entity may fulfil the disclosure objective by providing a reconciliation between the opening and closing balances in the Statement of Financial Position for liabilities arising from financing activities.

The following is a list of standards/interpretations that have been issued and are effective for accounting periods commencing on January 1, 2018 or January 1, 2019, as specified.

- *IFRS 9 - Financial Instruments*¹
- *IFRS 15 - Revenue from Contracts with Customers*¹
- *IFRIC 22 - Foreign Currency Transactions and Advance Consideration*¹
- *IFRS 16 - Leases*²

¹Effective for annual periods beginning on or after January 1, 2018, with earlier application permitted.

²Effective for annual periods beginning on or after January 1, 2019, with earlier application permitted.

4.1 IFRS 9 - Financial Instruments

In July 2014, the IASB finalized the reform of financial instruments accounting and issued IFRS 9 (as revised in 2014), which contains the requirements for a) the classification and measurement of financial assets and financial liabilities, b) impairment methodology, and c) general hedge accounting. IFRS 9 (as revised in 2014) will supersede IAS 39 - Financial Instruments: Recognition and Measurement upon its effective date.

Phase 1: Classification and measurement of financial assets and financial liabilities

With respect to classification and measurement, the number of categories of financial assets under IFRS 9 has been reduced; all recognized financial assets that are currently within the scope of IAS 39 will be subsequently measured at either amortized cost or fair value under IFRS 9.

IFRS 9 also contains requirements for the classification and measurement of financial liabilities and derecognition requirements.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

One major change from IAS 39 relates to the presentation of changes in the fair value of a financial liability designated as at FVTPL attributable to changes in the credit risk of that liability. Under IFRS 9, such changes are presented in other comprehensive income, unless the presentation of the effect of the change in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss.

Phase 2: Impairment of financial assets

The impairment model under IFRS 9 reflects expected credit losses, as opposed to incurred credit losses under IAS 39. Under the impairment approach in IFRS 9, it is no longer necessary for a credit event to have occurred before credit losses are recognized. Instead, an entity always accounts for expected credit losses and changes in those expected credit losses. The amount of expected credit losses should be updated at each reporting date to reflect changes in credit risk since initial recognition.

Phase 3: Hedge accounting

The general hedge accounting requirements of IFRS 9 retain the three types of hedge accounting mechanisms in IAS 39. However, greater flexibility has been introduced to the types of transactions eligible for hedge accounting. In addition, the effectiveness test has been overhauled and replaced with the principle of an 'economic relationship'. Retrospective assessment of hedge effectiveness is no longer required. Far more disclosure requirements about an entity's risk management activities have been introduced.

Transitional provisions

IFRS 9 (as revised in 2014) is effective for reporting periods beginning on or after January 1, 2018 with earlier application permitted. Management has elected to adopt the standard as of the effective date and although the classification of existing financial instruments and related disclosures will change, there will be no material adjustments to the amounts reported in Nalcor's annual audited consolidated financial statements.

4.2 IFRS 15 Revenue from Contracts with Customers

IFRS 15 establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. It will supersede the following revenue standards and interpretations upon its effective date:

- IAS 18 Revenue;
- IAS 11 Construction Contracts;
- IFRIC 13 Customer Loyalty Programs;
- IFRIC 15 Agreements for the Construction of Real Estate;
- IFRIC 18 Transfers of Assets from Customers; and
- SIC 31 Revenue-Barter Transactions Involving Advertising Services.

As suggested by the title of the new revenue standard, IFRS 15 will only cover revenue arising from contracts with customers. Under IFRS 15, a customer of an entity is a party that has contracted with the entity to obtain goods or services that are an output of the entity's ordinary activities in exchange for consideration. Unlike the scope of IAS 18, the recognition and measurement of interest income and dividend income from debt and equity investments are no longer within the scope of IFRS 15. Instead, they are within the scope of IAS 39 (or IFRS 9 if it is early adopted).

As mentioned above, the new standard has a single model to deal with revenue from contracts with customers. Its core principle is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

Specifically, the standard introduces a five-step approach to revenue recognition:

Step 1: Identify the contract(s) with a customer.

Step 2: Identify the performance obligations in the contract.

Step 3: Determine the transaction price.

Step 4: Allocate the transaction price to the performance obligations in the contract.

Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Extensive disclosures are also required by the new standard.

IFRS 15, together with clarifications thereto issued in April 2016, is effective for reporting periods beginning on or after January 1, 2018 with earlier application permitted. Management has elected to adopt the standard as of the effective date and although the related disclosures will change, there will be no material adjustments to the amounts reported in Nalcor's annual audited consolidated financial statements.

4.3 IFRIC 22 Foreign Currency Transactions and Advance Consideration

IFRIC 22 addresses how to determine the 'date of transaction' for the purpose of determining the exchange rate to use on initial recognition of an asset, expense or income, when consideration for that item has been paid or received in advance in a foreign currency which resulted in the recognition of a non-monetary asset or non-monetary liability (for example, a non-refundable deposit or deferred revenue).

The Interpretation is effective for reporting periods beginning on or after January 1, 2018 with earlier application permitted. Entities can apply the Interpretation either retrospectively or prospectively. Specific transition provisions apply to prospective application. The application of these amendments to IFRIC 22 will not have a material impact on Nalcor's annual audited consolidated financial statements.

4.4 IFRS 16 - Leases

IFRS 16 provides a comprehensive model for the identification of lease arrangements and their treatment in the financial statements of both lessees and lessors. It will supersede the following lease standard and interpretations upon its effective date:

- IAS 17 Leases;
- IFRIC 4 Determining Whether an Arrangement contains a Lease;
- SIC-15 Operating Leases – Incentives; and
- SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease.

IFRS 16 applies a control model to the identification of leases, distinguishing between leases and service contracts on the basis of whether there is an identified asset controlled by the customer.

The standard introduces significant changes to lessee accounting: it removes the distinction between operating and finance leases under IAS 17 and requires a lessee to recognize a right-of-use asset and a lease liability at lease commencement for all leases, except for short-term leases and leases of low value assets.

In contrast to lessee accounting, the IFRS 16 lessor accounting requirements remain largely unchanged from IAS 17, which continue to require a lessor to classify a lease as either an operating lease or a finance lease.

A lessee can apply IFRS 16 either by a full retrospective approach or a modified retrospective approach. If the latter approach is selected, an entity is not required to restate the comparative information and the cumulative effect of initially applying IFRS 16 must be presented as an adjustment to opening retained earnings. Management anticipates that the application of IFRS 16 in the future may have a material impact on the amounts reported and disclosures made in Nalcor's annual audited consolidated financial statements. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 16 until Management performs a detailed review.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

5. CASH AND CASH EQUIVALENTS

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Cash	143	130
Cash equivalents	-	13
	143	143

The effective interest rate on cash equivalents at December 31, 2017 was nil (2016 - 0.97%).

6. TRADE AND OTHER RECEIVABLES

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Trade receivables	199	148
Advances (a)	78	38
Other receivables (b)	135	124
Allowance for doubtful accounts	(17)	(16)
	395	294

(a) Advances relate to the current portion of long-term advances to suppliers in relation to construction of the Lower Churchill Project.

(b) Other receivables are comprised primarily of harmonized sales tax (HST) as well as interest on long-term investments.

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
0-60 days	365	247
60+ days	30	47
	395	294

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Allowance for doubtful accounts, beginning of year	(16)	(13)
Amounts provided for during the year	(1)	(3)
Allowance for doubtful accounts, end of year	(17)	(16)

As at December 31, 2017, trade and other receivables included balances of \$40.6 million (2016 - \$43.9 million) denominated in United States Dollars (USD).

7. INVENTORIES

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Materials and other	57	47
No. 6 fuel	48	35
Diesel fuel	4	4
Other fuel	4	5
Construction aggregates	3	2
	116	93

The cost of inventories recognized as an expense during the year is \$234.1 million (2016 - \$173.9 million) and is included in operating costs and fuels.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

8. PROPERTY, PLANT AND EQUIPMENT

<i>(millions of Canadian dollars)</i>	Generation Plant	Transmission and Distribution	Petroleum and Natural Gas Properties	Other	Construction in Progress	Total
Cost						
Balance at January 1, 2016	1,711	773	1,117	419	5,182	9,202
Additions	-	-	208	1	3,041	3,250
Disposals	(6)	(3)	-	(4)	-	(13)
Transfers	94	98	-	28	(220)	-
Decommissioning liabilities and revisions	(14)	1	(10)	-	-	(23)
Other adjustments	-	-	-	(2)	-	(2)
Balance at December 31, 2016	1,785	869	1,315	442	8,003	12,414
Additions	-	1	123	22	3,227	3,373
Disposals	(3)	(4)	(13)	(4)	-	(24)
Transfers	69	335	-	26	(430)	-
Decommissioning liabilities and revisions	(1)	-	2	-	-	1
Other adjustments	-	-	-	(2)	(13)	(15)
Balance at December 31, 2017	1,850	1,201	1,427	484	10,787	15,749
Depreciation, depletion and impairment						
Balance at January 1, 2016	412	140	172	153	-	877
Depreciation and depletion	48	23	40	14	-	125
Disposals	(2)	(1)	-	(2)	-	(5)
Balance at December 31, 2016	458	162	212	165	-	997
Depreciation and depletion	53	27	57	15	-	152
Disposals	(2)	(1)	-	(2)	-	(5)
Impairment	-	-	-	-	51	51
Balance at December 31, 2017	509	188	269	178	51	1,195
Carrying value						
Balance at January 1, 2016	1,299	633	945	266	5,182	8,325
Balance at December 31, 2016	1,327	707	1,103	277	8,003	11,417
Balance at December 31, 2017	1,341	1,013	1,158	306	10,736	14,554

Capitalized interest for the year ended December 31, 2017, was \$268.0 million (December 31, 2016 - \$198.3 million) related to assets under development.

As at December 31, 2017, construction in progress includes \$140.3 million (2016 - \$186.3 million) of capitalized Gull Island Project costs. This is subsequent to an impairment of \$50.6 million as at December 31, 2017 of the Gull Island Project relating to older costs, previously capitalized, which Management has assessed as no longer having future economic benefit towards the project.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

9. INTANGIBLE ASSETS

<i>(millions of Canadian dollars)</i>	Computer Software	Feasibility Studies	Seismic Data Acquisitions	Intellectual Property	Assets Under Development	Total
Cost						
Balance at January 1, 2016	16	2	41	2	-	61
Additions	-	-	28	-	8	36
Balance at December 31, 2016	16	2	69	2	8	97
Additions	-	-	37	-	14	51
Balance at December 31, 2017	16	2	106	2	22	148
Amortization and impairment						
Balance at January 1, 2016	7	1	3	-	-	11
Amortization	2	-	8	-	-	10
Balance at December 31, 2016	9	1	11	-	-	21
Amortization	2	-	14	-	-	16
Impairment	-	-	81	-	-	81
Balance at December 31, 2017	11	1	106	-	-	118
Carrying value						
Balance at January 1, 2016	9	1	38	2	-	50
Balance at December 31, 2016	7	1	58	2	8	76
Balance at December 31, 2017	5	1	-	2	22	30

As at December 31, 2017, intangible assets included an impairment expense of \$81.0 million related to seismic and geoscientific data acquisition costs previously capitalized as Management assessed the costs as having no short or medium-term future economic benefit to Nalcor.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

10. LONG-TERM INVESTMENTS

In July 2017, Muskrat Falls, Labrador Transco, and the IT purchased six 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 PFA and the LIL PFA.

<i>As at December 31 (millions of Canadian dollars)</i>	Year of Maturity	2017	2016
Muskrat Falls			
\$75.0 million Floating Rate Deposit Note, with interest paid at the one-month Canadian Dollar Offered Rate (CDOR) plus 0.38%.	2017	-	49
\$75.0 million Floating Rate Deposit Note, with interest paid at the one-month CDOR plus 0.20%.	2019	61	-
\$483.8 million Amortizing Floating Rate Deposit Note, with interest paid at the one-month CDOR plus 0.20%.	2019	266	-
\$725.7 million Amortizing Fixed Rate Deposit Note, with interest paid at a rate of 1.679% per annum.	2019	400	-
Labrador Transco			
\$75.0 million Floating Rate Deposit Note, with interest paid at the one-month CDOR plus 0.38%.	2017	-	13
\$75.0 million Floating Rate Deposit Note, with interest paid at the one-month CDOR plus 0.20%.	2019	14	-
\$483.8 million Amortizing Floating Rate Deposit Note, with interest paid at the one-month CDOR plus 0.20%.	2019	62	-
\$725.7 million Amortizing Fixed Rate Deposit Note, with interest paid at a rate of 1.679% per annum.	2019	94	-
LIL			
\$75.0 million Floating Rate Deposit Note, with interest paid at the one-month CDOR plus 0.38%.	2017	-	29
\$75.0 million Floating Rate Deposit Note, with interest paid at the one-month CDOR plus 0.20%.	2019	75	-
\$182.9 million Amortizing Floating Rate Deposit Note, with interest paid at the one-month CDOR plus 0.20%.	2019	91	-
\$548.6 million Amortizing Fixed Rate Deposit Note, with interest paid at a rate of 1.644% per annum.	2019	273	-
Churchill Falls			
\$18.4 million Redeemable Guaranteed Investment Certificate (GIC), with interest paid at a rate of 1.40% per annum.	2019	18	18
\$15.5 million Redeemable GIC, with interest paid at a rate of 1.46% per annum.	2019	16	16
Total long-term investments		1,370	125
Less: redemptions to be received within the next year ¹		(1,038)	(91)
		332	34

¹Redemptions to be received within one year have been reclassified to short-term investments.

As at December 31, 2017, Churchill Falls held a bank deposit note purchased on October 25, 2017 for \$22.1 million maturing April 25, 2018 with an interest rate of 1.52% per annum. Nalcor's 65.8% share of the short-term investment is \$14.5 million (2016 - \$nil).

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

11. OTHER LONG-TERM ASSETS

<i>As at December 31 (millions of Canadian dollars)</i>		2017	2016
Investment property	(a)	1	1
Investment in joint arrangement		1	1
Long-term receivables	(b)	-	28
Long-term prepayments		1	3
Reserve fund	(c)	-	15
Sinking funds	(d)	231	307
Other		1	1
Other long-term assets		235	356
Less: current portion		(2)	(82)
		233	274

- (a) As at December 31, 2017, the fair value measurement of the investment property is categorized as a Level 3 valuation. The fair value of the investment property at December 31, 2017 is estimated to be \$1.9 million (2016 - \$19.4 million). Due to the nature of the property and lack of comparable market data, the fair value of Nalcor's investment property is determined using the present value of future cash flows. Nalcor's 2017 estimate is based on cash flows estimated to occur between 2018 and 2022, discounted at a rate of 12.0%.
- (b) As at December 31, 2017, long-term receivables include \$nil (2016 - \$26.9 million) related to long-term advances to suppliers in relation to construction of the Lower Churchill Project. The current portion of \$77.6 million (2016 - \$38.2 million) is included in trade and other receivables. The non-current portion of receivables associated with customer payment plans and the long-term portion of employee purchase programs as at December 31, 2017 is \$0.3 million (2016 - \$0.5 million).
- (c) In 2007 Churchill Falls commenced the creation of a \$75.0 million segregated reserve fund pursuant to the terms of the Shareholders' Agreement to contribute towards the funding of capital expenditures related to Churchill Falls' existing facilities and their replacement. Churchill Falls invested \$17.0 million in each of 2007, 2008 and 2009 and \$8.0 million in each of 2010, 2011 and 2012. In December 2017, \$22.5 million (2016 - \$23.4 million) was withdrawn to fund a portion of capital expenditures. As per the terms of the Shareholders' Agreement, these funds will be replaced over a five year period beginning in 2018.

This fund must remain in place until the end of the Shareholders' Agreement in 2041. Any amounts removed to fund capital expenditures must be replaced. Reserve fund holdings consist of securities issued by the Government of Canada, various provinces of Canada and Schedule 1 and 2 Canadian Chartered Banks.

Nalcor's proportionate share of the reserve fund consists of the following:

<i>As at December 31 (millions of Canadian dollars)</i>		2017	2016
Reserve fund, beginning of year		15	31
Principal withdrawals		(15)	(16)
Reserve fund, end of year		-	15
Less: current portion		-	(5)
		-	10

Nalcor's proportionate share of reserve fund contributions for the next five years are as follows:

<i>(millions of Canadian dollars)</i>	2018	2019	2020	2021	2022
Reserve fund contributions	12	12	12	6	7

- (d) As at December 31, 2017, sinking funds include \$190.2 million (2016 - \$267.0 million) related to repayment of Hydro's long-term debt and \$40.9 million (2016 - \$40.1 million) related to funding of Nalcor's long-term payable under the Upper Churchill

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Redress Agreement (UCRA). Sinking fund investments consist of bonds, debentures, promissory notes and coupons issued by, or guaranteed by, the Government of Canada, provincial governments or Schedule 1 banks, and have maturity dates ranging from 2018 to 2041.

Hydro debentures, which are intended to be held to maturity, are deducted from debt while all other sinking fund investments are shown separately on the Consolidated Statement of Financial Position as assets. Annual contributions to the various sinking funds are in accordance with bond indenture terms, and are structured to ensure the availability of adequate funds at the time of expected bond redemption. Effective yields range from 2.57% to 6.82% (2016 - 0.97% to 9.12%).

Nalcor's sinking funds are held to fund the annual payments to the Innu Nation as required under the UCRA.

The sinking funds consist of the following:

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Sinking funds, beginning of year	307	284
Contributions	7	8
Earnings	24	14
Disposals and maturities	(97)	(2)
Mark-to-market adjustment	(10)	3
Sinking funds, end of year	231	307
Less: current portion	(2)	(77)
	229	230

Sinking fund instalments due for the next five years are as follows:

<i>(millions of Canadian dollars)</i>	2018	2019	2020	2021	2022
Sinking fund instalments	7	7	7	7	7

12. REGULATORY DEFERRALS

<i>As at (millions of Canadian dollars)</i>	January 1 2017	Reclass and Disposition	Regulatory Activity	December 31 2017	Remaining Recovery Settlement Period (years)
Regulatory asset deferrals					
2014 cost deferral (a)	39	(38)	(1)	-	n/a
2015 cost deferral (b)	25	(28)	3	-	n/a
2016 cost deferral (c)	32	(36)	4	-	n/a
Deferred energy conservation costs (e)	8	-	1	9	n/a
Deferred foreign exchange on fuel (f)	-	-	(1)	(1)	n/a
Deferred lease costs (g)	5	-	(1)	4	3.4
Energy supply deferral (j)	-	31	21	52	n/a
Foreign exchange losses (k)	54	-	(2)	52	24.0
Phase Two hearing costs (p)	1	-	-	1	n/a
Other (d),(m)	-	-	-	-	n/a
	164	(71)	24	117	
Regulatory liability deferrals					
Insurance amortization and proceeds (n)	(4)	-	1	(3)	n/a
Labrador refund (o)	-	(1)	-	(1)	2.0
Rate stabilization plan (RSP) (q)	(344)	203	66	(75)	n/a
Other (h)	-	-	-	-	n/a
	(348)	202	67	(79)	

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

12.1 Regulatory Adjustments Recorded in the Consolidated Statement of Profit and Comprehensive (Loss) Income

The following table shows Hydro's regulatory deferrals which will be, or are expected to be, reflected in customer rates in future periods and have been established through the rate setting process. In the absence of rate regulation, these amounts would be reflected in operating results in the period and the profit for the period ended December 31, 2017 would have decreased by \$91.1 million (2016 - a decrease of \$0.8 million).

<i>For the year ended December 31 (millions of Canadian dollars)</i>		2017	2016
RSP amortization		(53)	(40)
RSP fuel deferral		(19)	42
RSP interest		9	25
Rural rate adjustment		(3)	(8)
Total RSP activity	(q)	(66)	19
2014 cost deferral	(a)	1	8
2015 cost deferral	(b)	(3)	2
2016 cost deferral	(c)	(4)	(32)
Deferred energy conservation	(e)	(1)	(1)
Deferred foreign exchange on fuel	(f)	1	1
Deferred lease costs	(g)	1	1
Energy supply deferral	(j)	(21)	-
Amortization of deferred foreign exchange losses	(k)	2	2
Fuel supply deferral	(l)	-	1
Insurance amortization and proceeds	(n)	(1)	(1)
Phase Two hearing costs	(p)	-	(1)
Other	(d),(h),(i),(m),(o)	-	-
		(91)	(1)

(a) 2014 Cost Deferral

In Board Order No. P.U. 22 (2017), the Board approved \$37.7 million of the \$38.7 million 2014 cost deferral, resulting in a loss in 2017 of \$1.0 million (2016 - \$8.0 million loss), and the disposition of the deferral balance from the RSP.

(b) 2015 Cost Deferral

In Board Order No. P.U. 22 (2017), the Board approved \$27.7 million of the 2015 cost deferral, resulting in a gain in 2017 of \$3.2 million (2016 - \$1.6 million loss), and the disposition of the deferral balance from the RSP.

(c) 2016 Cost Deferral

The 2016 cost deferral of \$32.4 million consisted of energy supply costs of \$31.0 million and other costs of \$1.4 million. As a result of Board Order No. P.U. 22 (2017), \$31.0 million was re-classified to the energy supply deferral. The Board also approved other 2016 costs of \$5.0 million, which resulted in an increase in profit of \$3.6 million in 2017, and the disposition of the deferral balance from the RSP.

(d) Asset Disposal

As per Board Order No. P.U. 49 (2016), the PUB Ordered that Hydro recognize a regulatory asset of \$0.4 million related to the Sunnyside transformer that was disposed of in 2014. Hydro is required to recover the deferred asset in rate base and amortize the asset for 22.4 years commencing in 2015. Hydro is required to exclude the new Sunnyside transformer from rate base until the Sunnyside Transformer Original Asset Deferral has been fully amortized.

(e) Deferred Energy Conservation

In 2017, Hydro deferred \$1.5 million (2016 - \$1.1 million) in the Energy Conservation Costs regulatory asset associated with an electrical conservation program for residential, industrial, and commercial sectors. In addition, as per Board Order No. P.U. 22 (2017), Hydro recovered \$0.5 million (2016 - \$nil) of the balance through a rate rider.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

- (f) **Deferred Foreign Exchange on Fuel**
Hydro purchases a significant amount of fuel for Holyrood Thermal Generating Station (HTGS) in USD. The RSP allows Hydro to defer variances in fuel prices (including foreign exchange fluctuations). During 2017, Hydro recognized in regulatory assets, foreign exchange gains on fuel purchases of \$0.4 million (2016 - \$0.9 million gain).
- (g) **Deferred Lease Costs**
In 2017, pursuant to Board Order No. P.U. 38 (2013), Board Order No. P.U. 17 (2016) and Board Order No. P.U. 23 (2016), Hydro deferred lease costs of \$nil (2016 - \$1.6 million) for diesel units and other necessary infrastructure to ensure black start capability at HTGS. In Board Order No. P.U. 17 (2016), Board Order No. P.U. 23 (2016) and Board Order No. P.U. 49 (2016) the Board approved the amortization of diesel units at (HTGS) over a period of five years. In 2017, Hydro recorded amortization of \$1.3 million (2016 - \$2.2 million) of the deferred lease costs.
- (h) **Deferred Purchased Power Savings**
In 1997, the PUB ordered Hydro to defer \$1.1 million related to reduced purchased power rates resulting from the interconnection of communities in the area of L'Anse au Clair to Red Bay to the Hydro-Québec system and amortize the balance over a 30 year period. The remaining unamortized savings in the amount of \$0.4 million (2016 - \$0.4 million) are deferred as a regulatory liability.
- (i) **Employee Future Benefits Actuarial Loss**
Pursuant to Board Order No. P.U. 36 (2015), Hydro has recognized the amortization of employee future benefit actuarial gains and losses in net income. During 2017, Hydro recorded \$0.1 million (2016 - \$0.2 million) employee future benefits losses as a regulatory adjustment. In the absence of rate regulation, IFRS would require Hydro to include employee future benefits actuarial gains and losses in other comprehensive loss. As a result, during 2017 Hydro also recorded a decrease of \$0.1 million (2016 - \$0.2 million) to other comprehensive loss to recognize the amount that was reclassified to profit or loss.
- (j) **Energy Supply Deferrals**
Pursuant to Board Order No. P.U. 22(2017), the Board approved the deferral of Energy Supply deferrals which includes the Energy Supply, Holyrood Conversion and Isolated Systems Supply deferral. The recovery of the deferral is subject to a future Board order. In 2017, \$31.0 million relating to energy supply deferred for the periods 2015-2016 was re-classified from the 2016 Cost deferral to the Energy Supply deferral. The net increase to profit in 2017 was \$21.3 million.
- (k) **Foreign Exchange Losses**
In 2002, the PUB ordered Hydro to defer realized foreign exchange losses related to the issuance of Swiss Franc and Japanese Yen denominated debt and amortize the balance over a 40 year period. Accordingly, these costs were recognized as a regulatory asset. During 2017, the amortization of \$2.2 million (2016 - \$2.2 million) reduced regulatory assets.
- (l) **Fuel Supply Deferral**
Pursuant to Board Order No. P.U. 56 (2014), Hydro received approval in 2014 to defer \$9.6 million as a regulatory asset in additional capacity related supply costs incurred during the three months ended March 31, 2014. As per Board Order No. P.U. 13 (2016) and Board Order No. P.U. 49 (2016), Hydro recorded a reduction of \$1.5 million in 2016 based upon the results of a Prudence Review. In 2016, as per Board Order No. P.U. 49 (2016), the remaining balance of \$8.1 million was re-classified to the 2014 Cost Deferral.
- (m) **Hearing Costs**
As per Board Order No. P.U. 49 (2016), the Board approved \$0.8 million in hearing costs to be deferred and amortized over a three year period commencing 2015. In 2017, Hydro recorded amortization of \$0.3 million (2016 - \$0.5 million).
- (n) **Insurance Amortization and Proceeds**
Pursuant to Board Order No. P.U. 13 (2012), Hydro records net insurance proceeds against the capital costs and amortizes the balance over the life of the asset. Under IFRS, Hydro is required to recognize the insurance proceeds and corresponding

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

amortization in regulatory liabilities. During 2017, Hydro recorded a decrease to regulatory liabilities resulting from amortization of \$0.5 million (2016 - \$0.6 million) related to the assets.

(o) Labrador Refund

Pursuant to Board Order No. P.U. 22 (2017), during 2017 Hydro refunded Labrador Industrial Transmission customers' excess revenues relating to the period of 2014 to 2017. The PUB also ordered that Hydro apply a rate reduction for a 30-month period to address excess revenues relating to Hydro's rural customers on the Labrador Interconnected System. In July 2017, Hydro began the amortization of excess revenues which resulted in a decrease to profit of \$0.5 million (2016 - \$nil).

(p) Phase Two Hearing Costs

Pursuant to Board Order No. P.U. 13 (2016), Hydro received approval to defer consulting fees, salary transfers and overtime relating to Phase Two of the investigation into the reliability and adequacy of power on the Island Interconnected system after the interconnection with the Muskrat Falls generating station. As a result, Hydro recorded a regulatory asset of \$0.3 million (2016 - \$0.9 million).

(q) RSP

In 1986, the PUB ordered Hydro to implement the RSP which primarily provides for the deferral of fuel expense variances resulting from changes in fuel prices, hydrology and load and associated interest. Additionally, the RSP also includes costs associated with the island interconnected and isolated systems. Adjustments required in utility rates to cover the amortization of the balance are implemented on July 1 of each year. Similar adjustments required in industrial rates are implemented on January 1 of each year. On June 30, 2017, the PUB approved rates for Hydro's Island Interconnected and Rural customers in Board Order No. P.U. 25 (2017).

During 2017, Hydro recorded a net decrease in regulatory liabilities of \$269.4 million (2016 - increase of \$19.0 million) resulting in an RSP ending balance for 2017 of \$74.2 million (2016 - \$343.6 million). The decrease in the RSP balance is primarily caused by the RSP surplus payout, the disposition of the 2014-2016 Cost Deferrals and GRA related payments, and the normal operation of the RSP. As per Board Order P.U. 36 (2016), the RSP was reduced by \$130.8 million relating to the refund of the utility surplus balance. The reduction was comprised of \$128.8 million refund to customers and \$2.0 million in administrative costs. The remaining portion of the utility surplus balance is \$12.6 million (2016 - \$143.4 million). As per Board Order No. P.U. 22 (2017) and Board Order No. P.U. 24 (2017), the Board approved a \$72.4 million recovery of the 2014-2016 Cost Deferrals and other GRA related payments through the RSP. The normal operation of the RSP resulted in an increase to net income of \$66.2 million (2016 - decrease of \$19.0 million).

13. TRADE AND OTHER PAYABLES

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Trade payables and accruals	491	1,089
Accrued interest payable	55	44
Rent and royalty payable	4	5
Other payables	34	24
	584	1,162

As at December 31, 2017, trade and other payables included balances of \$23.5 million (2016 - \$34.2 million) denominated in USD, \$nil (2016 - \$0.1 million) denominated in Great British Pounds and \$0.9 million (2016 - \$45.0 million) denominated in Euros.

14. DEBT

14.1 Short-term Borrowings

Nalcor maintains a \$250.0 million CAD or USD equivalent committed revolving term credit facility with its banker, with a maturity

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

date of January 31, 2019. There were no amounts drawn on this facility as at December 31, 2017 (2016 - \$nil), however \$34.3 million of the borrowing limit has been used to issue 15 irrevocable letters of credit (2016 - \$34.1 million). Borrowings in CAD may take the form of Prime Rate Advances, Bankers' Acceptances (BAs) and letters of credit. Borrowings in USD may take the form of Base Rate Advances, London Interbank Offer Rate (LIBOR) Advances and letters of credit. The facility also provides coverage for overdrafts on Nalcor's bank accounts, with interest calculated at the Prime Rate.

Two letters of credit, totaling \$25.7 million, are on behalf of Oil and Gas to ensure compliance with regulations relating to petroleum and natural gas exploration and production activities. Another 12 letters, totaling \$7.8 million, are on behalf of Energy Marketing and relate to power purchases and sale contracts with various independent system operators, transmission providers and bilateral counterparties. One irrevocable letter of credit for \$0.8 million was issued by Nalcor in July 2017 as bid security for a Request for Proposal (RFP) for the supply of energy.

In December 2017, Nalcor, on behalf of Energy Marketing, issued an unconditional guarantee in the amount of \$10.0 million, in order to guarantee amounts under a power purchase and sale contract with a bilateral counterparty.

On September 29, 2017, Nalcor refinanced the \$225.0 million promissory note to the Province dated March 31, 2017. The new promissory note matures March 30, 2018 and carries an interest rate of 1.845%.

On July 27, 2017, Hydro converted its \$50.0 million demand operating facility, to a \$200.0 million CAD or USD equivalent committed revolving term credit facility, with a maturity date of July 27, 2019. As at December 31, 2017, there were no amounts drawn on the facility (2016 - \$nil). Borrowings in CAD may take the form of Prime Rate Advances, BAs and letters of credit, with interest calculated at the Prime Rate or prevailing Government BA fee. Borrowings in USD may take the form of Base Rate Advances, LIBOR Advances and letters of credit. The facility also provides coverage for overdrafts on Hydro's bank accounts, with interest calculated at the Prime Rate.

In addition, Hydro utilized its government guaranteed promissory note program to fulfil its short-term funding requirements. As at December 31, 2017, there were \$144.0 million in promissory notes outstanding with a maturity date of January 3, 2018 bearing an interest rate of 1.13% (2016 - \$210.0 million bearing an interest rate of 0.63%). Upon maturity, a promissory note was reissued in the amount of \$155.0 million with a maturity date of January 16, 2018 bearing an interest rate of 1.17%.

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Promissory notes - borrowed from the Province	225	225
Promissory notes - borrowed from external markets	144	210
	369	435

Churchill Falls maintains a \$10.0 million Canadian or US equivalent unsecured operating credit facility with its banker. Advances may take the form of a Prime Rate advance or the issuance of a BA with interest calculated at the Prime Rate or prevailing Government BA Fee. The facility provides coverage for overdrafts on Churchill Falls' bank accounts, with interest calculated at the Prime Rate. There were no amounts drawn on this facility as at December 31, 2017 (2016 - \$nil).

Churchill Falls has issued three irrevocable letters of credit totaling \$2.0 million (2016 - \$2.0 million), \$1.0 million of which does not impact the borrowing limit of the operating credit facility (2016 - \$1.0 million). The letters of credit ensure satisfactory management of its waste management system and compliance with a certificate of approval for the transportation of special and hazardous wastes, granted by the Provincial Department of Environment and Conservation.

Oil and Gas maintains a \$30.0 million CAD or USD equivalent unsecured credit facility with its banker and as at December 31, 2017, there were no amounts drawn on this facility (2016 - \$nil), however \$5.4 million of the borrowing limit has been used to issue two irrevocable letters of credit (2016 - \$0.5 million). Borrowings in CAD may take the form of Prime Rate Advances and letters of credit. Borrowings in USD may take the form of Base Rate Advances and letters of credit. In April 2017, Oil and Gas issued an irrevocable letter of credit in the amount of \$4.9 million to the Canada-Newfoundland and Labrador Offshore Petroleum Board (C-NLOPB). The purpose of the letter was to provide proof of financial responsibility with respect to the Hebron project.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Energy Marketing maintains a \$20.0 million CAD or USD equivalent demand operating credit facility with its banker, and as at December 31, 2017, there were no amounts drawn on this facility (2016 - \$nil). This facility has an unconditional and irrevocable guarantee from Nalcor. Borrowings in CAD may take the form of Prime Rate Advances, BAs and letters of credit. Borrowings in USD may take the form of Base Rate Advances, LIBOR Advances and letters of credit.

14.2 Long-term Debt

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

<i>As at December 31 (millions of Canadian dollars)</i>	Face Value	Coupon Rate %	Year of Issue	Year of Maturity	2017	2016
Hydro						
X*	-	10.25	1992	2017	-	150
Y*	300	8.40	1996	2026	295	295
AB*	300	6.65	2001	2031	305	306
AD*	125	5.70	2003	2033	124	124
AF	500	3.60	2014/2017	2045	480	197
1A	300	3.70	2017	2048	330	-
LIL LP						
Tranche A	725	3.76	2013	2033	726	726
Tranche B	600	3.86	2013	2045	600	600
Tranche C	1,075	3.85	2013	2053	1,075	1,075
Tranche 1-10	105	1.14-1.75	2017	2020-2025	105	-
Tranche 11-20	105	1.84-2.37	2017	2025-2030	105	-
Tranche 21-30	105	2.41-2.64	2017	2030-2035	105	-
Tranche 31-40	105	2.66-2.80	2017	2035-2040	105	-
Tranche 41-50	105	2.81-2.86	2017	2040-2045	105	-
Tranche 51-60	105	2.84-2.86	2017	2045-2050	105	-
Tranche 61-70	105	2.85	2017	2050-2055	105	-
Tranche 71-74	315	2.85	2017	2055-2057	316	-
Lab Transco/Muskrat Falls						
Tranche A	650	3.63	2013	2029	650	650
Tranche B	675	3.83	2013	2037	675	675
Tranche C	1,275	3.86	2013	2048	1,275	1,275
Tranche 1-10	205	1.14-1.75	2017	2020-2025	205	-
Tranche 11-20	224	1.84-2.37	2017	2025-2030	224	-
Tranche 21-30	253	2.41-2.64	2017	2030-2035	253	-
Tranche 31-40	288	2.66-2.80	2017	2035-2040	289	-
Tranche 41-50	331	2.81-2.86	2017	2040-2045	331	-
Tranche 51-60	381	2.84-2.86	2017	2045-2050	382	-
Tranche 61-64	168	2.85	2017	2050-2052	168	-
Total	9,425				9,438	6,073
Less: Sinking fund investments in own debentures					45	57
					9,393	6,016
Less: maturities of debt within one year					-	150
Less: sinking fund payments within one year					7	7
Less: maturities of sinking funds in own debentures					-	(14)
					9,386	5,873

*Sinking funds have been established for these issues.

Hydro's promissory notes and long-term debt are unsecured and unconditionally guaranteed as to principal and interest and,

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

where applicable, sinking fund payments, by the Province, with the exception to Series 1A. The Province charges Hydro a guarantee fee of 25 basis points annually on the total debt (net of sinking funds) with a remaining term to maturity of less than or equal to 10 years and 50 basis points annually on total debt (net of sinking funds) with a remaining term to maturity greater than 10 years for debt outstanding as of December 31, 2010. For debt issued subsequent to December 31, 2010, the guarantee rate is 25 basis points annually on the total debt (net of sinking funds) with an original term to maturity of less than or equal to 10 years and 50 basis points annually on total debt (net of sinking funds) with an original term to maturity greater than 10 years. The guarantee fee charged by the Province for the year ended December 31, 2017 was \$4.1 million (2016 - \$4.5 million).

On January 20, 2017, Hydro issued new long-term debt through the reopening and sale of \$300.0 million of Series AF debentures to its underwriting syndicate. The debentures mature on December 1, 2045 with a coupon rate of 3.60% paid semi-annually.

On July 14, 2017 Hydro's \$150.0 million long-term debt, Series X, matured. Sinking fund disposals during the year in the amount of \$95.1 million were used to offset the Series X maturity.

On December 20, 2017, Hydro issued new long-term debt, Series 1A, with a face value of \$300.0 million. The Province of Newfoundland and Labrador issued debt specifically on Hydro's behalf and lent the proceeds to Hydro. The debt matures on October 17, 2048 with a coupon rate of 3.70% paid semi-annually.

On January 3, 2018, Hydro reissued a promissory note in the amount of \$155.0 million with a maturity date of January 16, 2018 bearing an interest rate of 1.17%. Upon maturity, the promissory note was reissued.

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 a series of 64 bonds with maturities 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.

On May 10, 2017, the IT, LIL Funding Trust, LIL LP, LIL Opco and the Collateral Agent executed second amendments to the IT Project Finance Agreement (IT PFA) and LIL PFA. Under the terms and conditions of the second amended IT PFA, the LIL Funding Trust agreed to provide an additional non-revolving credit facility in the amount of \$1.05 billion to the IT. These facilities, available in a series of 74 bonds with maturities every six months beginning in December 2020, were fully drawn down 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.

The financing of the MF/LTA Funding Trust and 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). Under the terms of the additional guarantee from the Government of Canada, Muskrat Falls, Labrador Transco and LIL LP agree to pay an annual guarantee fee starting in May 2018 equal to 0.5% of the average balance outstanding on LIL LP Tranches 1 through 74 and Labrador Transco/Muskrat Falls Tranches 1 through 64 for the prior twelve months.

As security for these debt obligations, Muskrat Falls, Labrador Transco and LIL LP have granted to the Collateral Agent first ranking liens on all present and future assets. Sinking funds, beginning in December 2020, are required to be set up for Tranche A, B and C debentures and are to be held in a sinking fund account under the control of the Collateral Agent.

15. CLASS B LIMITED PARTNERSHIP UNITS

Debt and equity instruments issued by LIL LP 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.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

The Class B limited partnership units represent Emera NL's ownership interest in the Partnership. As described in the 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. The return on the units is classified as a finance expense. All finance expenses associated with the units have been capitalized.

<i>As at December 31 (millions of Canadian dollars)</i>	Units	2017	Units	2016
Class B limited partnership units, beginning of year	25	399	25	207
Contributions	-	55	-	168
Accrued interest	-	37	-	24
Class B limited partnership units, end of year	25	491	25	399

16. DEFERRED CREDITS

Deferred credits consist of funding from the Province, deferred energy sales to Emera NL and deferred lease revenue related to Menihek lease assets for the sale of energy to Hydro-Québec.

<i>As at December 31, 2017 (millions of Canadian dollars)</i>	Government Funding	Oil and Gas Over-lift	Deferred Energy Sales	Deferred Lease Revenue	Total
Deferred credits, beginning of year	2	1	1,145	16	1,164
Additions	1	-	588	5	594
Amortization	(2)	-	-	(3)	(5)
Deferred credits, end of year	1	1	1,733	18	1,753
Less: current portion	(1)	-	-	-	(1)
	-	1	1,733	18	1,752

Nalcor has received funding from the Province for wind feasibility studies in Labrador. The funding is recognized as other revenue when the related expenditures are incurred.

Nalcor has also received funding from the Province towards two Oil and Gas initiatives. The first is the Petroleum Exploration Enhancement Program (PEEP) which is designed to boost new petroleum exploration in Western Newfoundland through acquisition and assessment of seismic data. The second is the Offshore Geoscience Data Project (OGDP) which is designed to encourage new offshore petroleum exploration in Newfoundland and Labrador through the acquisition and assessment of seismic data. The funding is recognized as other revenue when the related expenditures are incurred. Deferred revenue also includes the over-lift position associated with Nalcor's net working interest of petroleum and natural gas produced, and the fair value of oil inventory held at the Newfoundland Transshipment site.

Nalcor has recorded deferred energy sales of \$1,732.9 million (2016 - \$1,144.5 million) which equals the construction costs to date incurred by Emera related to the Maritime Link. Nalcor has determined that it controls the Maritime Link asset for financial reporting purposes, and as such, has recorded the costs as a component of property, plant and equipment under construction.

Deferred lease revenue includes deferred lease revenue related to the Menihek plant.

17. DEFERRED CONTRIBUTIONS

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Deferred contributions, beginning of year	12	12
Additions	1	1
Amortization	(1)	(1)
Deferred contributions, end of year	12	12
Less: current portion	(1)	(1)
	11	11

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

18. DECOMMISSIONING LIABILITIES

Nalcor has recognized liabilities associated with the retirement of portions of the HTGS, disposal of Polychlorinated Biphenyls (PCB) and decommissioning liabilities resulting from its net ownership interests in petroleum and natural gas properties and related well sites.

The reconciliation of beginning and ending carrying amounts of decommissioning liabilities as at December 31, 2017 and December 31, 2016 are as follows:

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Decommissioning liabilities, beginning of year	83	103
Liabilities settled	(1)	(1)
Accretion	3	4
Revisions	1	(23)
<u>Decommissioning liabilities, end of year</u>	<u>86</u>	<u>83</u>
<u>Less: current portion</u>	<u>-</u>	<u>(1)</u>
	<u>86</u>	<u>82</u>

The total estimated undiscounted cash flows required to settle the HTGS obligations as at December 31, 2017 are \$15.2 million (2016 - \$15.2 million). In 2016, the HTGS decommissioning obligation decreased primarily due to an updated assumption that Holyrood will be used as an industrial site for the foreseeable future because of the operation of assets such as the Holyrood CT and the black start diesels. Payments to settle the liabilities are expected to occur between 2020 and 2023. The fair value of the decommissioning liabilities was determined using the present value of future cash flows discounted at Hydro's credit adjusted risk free rate of 2.6% (2016 - 2.5%). Nalcor has recorded \$13.5 million (2016 - \$13.4 million) related to HTGS obligations.

The total estimated undiscounted cash flows required to settle the PCB obligations as at December 31, 2017 are \$1.8 million (2016 - \$2.7 million). Payments to settle the liabilities are expected to occur between 2018 and 2025. The fair value of the decommissioning liabilities was determined using the present value of future cash flows discounted at Hydro's and Churchill Falls' credit adjusted risk free rates of 2.8% to 3.2%, respectively, (2016 - 2.9% to 3.7%). Nalcor has recorded \$1.5 million (2016 - \$2.4 million) related to PCB obligations.

Oil and Gas' decommissioning liabilities result from net ownership interests in petroleum and natural gas properties and related well sites. The total undiscounted estimated cash flows required to settle the obligations, including a rate of inflation of 2%, at December 31, 2017 are \$131.3 million (2016 - \$116.8 million). Payments to settle the liabilities are expected to occur between 2028 and 2033. The fair value of the decommissioning liabilities was determined using the present value of future cash flows discounted at rates ranging from 3.9% to 4.2% (December 31, 2016 - 4.0% to 4.3%).

A significant number of Nalcor's assets include generation plants, transmission assets and distribution systems. These assets can continue to run indefinitely with ongoing maintenance activities. As it is expected that Nalcor's assets will be used for an indefinite period, no removal date can be determined and consequently, a reasonable estimate of the fair value of any related decommissioning liability cannot be determined at this time. If it becomes possible to estimate the fair value of the cost of removing assets that Nalcor is required to remove, a decommissioning liability for those assets will be recognized at that time.

19. LONG-TERM PAYABLES

As at December 31, 2017, long-term payables consist of a payable to the Innu Nation under the UCRA, a payable to the Innu Nation under the Impact and Benefits Agreement (IBA) and a payable to the NunatuKavut Community Council under the Community Development Agreement (CDA).

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Long-term payables, beginning of year	65	77
Payments	(7)	(15)
Additions and revisions	(1)	-
Accretion	4	3
	61	65
Less: current portion	(9)	(7)
Long-term payables, end of year	52	58

Under the UCRA, Nalcor is required to pay to the Innu Nation \$2.0 million annually, escalating by 2.5% annually until 2041. At December 31, 2017, \$2.4 million (2016 - \$2.2 million) of the amount is current and is recorded in trade and other payables. Nalcor has sinking funds in the amount of \$40.9 million (2016 - \$40.1 million) to fund these future obligations.

Under the IBA, Nalcor is required to make annual implementation payments to the Innu Nation that commenced upon sanction of the Muskrat Falls hydroelectric plant. The Muskrat Falls hydroelectric plant was sanctioned in December 2012 and the first IBA payment was made at that time. The IBA requires annual payments of \$5.0 million escalating by an annual consumer price index from sanction until the earlier of first commercial power or ten years. The present value of the remaining payments using a discount rate of 2.9% (2016 - 2.7%) is \$13.2 million (2016 - \$27.9 million). The current portion of the payable at December 31, 2017 is \$5.0 million (2016 - \$5.0 million) and is recorded in trade and other payables.

Under the CDA signed on December 1, 2017, Nalcor is required to pay the NunatuKavut Community Council for the obligations as outlined in the agreement. At December 31, 2017, the present value of the payable is \$7.5 million. The current portion of the payable as at December 31, 2017 is \$1.5 million and is recorded in trade and other payables.

20. EMPLOYEE FUTURE BENEFITS

20.1 Pension Plan

Employees participate in the Province's Public Service Pension Plan, a multi-employer defined benefit plan. The employer's contributions of \$13.1 million (2016 - \$12.0 million) are expensed as incurred.

20.2 Other Benefits

Nalcor provides group life insurance and health care benefits on a cost shared basis to retired employees, and in certain cases, their surviving spouses, in addition to a retirement allowance. In 2017, cash payments to beneficiaries for its unfunded other employee future benefits were \$4.5 million (2016 - \$8.9 million). An actuarial valuation was performed as at December 31, 2017.

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Accrued benefit obligation, beginning of year	117	116
Current service cost	5	5
Interest cost	5	5
Benefits paid	(4)	(9)
Actuarial loss	3	-
Accrued benefit obligation, end of year	126	117

<i>For the year ended December 31 (millions of Canadian dollars)</i>	2017	2016
Component of benefit cost		
Current service cost	5	5
Interest cost	5	5
Total benefit expense for the year	10	10

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

The significant actuarial assumptions used in measuring the accrued benefit obligations and benefit expenses are as follows:

	2017	2016
Discount rate - benefit cost	3.90%	4.10%
Discount rate - accrued benefit obligation	3.55%	3.90%
Rate of compensation increase	3.50%	3.50%

Assumed healthcare trend rates:

	2017	2016
Initial health care expense trend rate	6.00%	5.85%
Cost trend decline to	4.50%	4.50%
Year that rate reaches the rate it is assumed to remain at	2028	2025

A 1% change in assumed health care trend rates would have had the following effects:

<i>Increase (millions of Canadian dollars)</i>	2017	2016
Current service and interest cost	2.5	2.1
Accrued benefit obligation	21.4	19.3
<i>Decrease (millions of Canadian dollars)</i>	2017	2016
Current service and interest cost	(1.8)	(1.5)
Accrued benefit obligation	(16.2)	(14.8)

21. SHAREHOLDER'S EQUITY

21.1 Share Capital

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Common shares of par value \$1 each		
Authorized - unlimited		
Issued and outstanding - 122,500,000	123	123

21.2 Shareholder Contributions

<i>As at December 31 (millions of Canadian dollars)</i>	2017	2016
Total shareholder contributions	3,693	2,861

During 2017, Nalcor's shareholder contributed capital in the amount of \$832.3 million (2016 - \$656.1 million) in relation to Nalcor's capital expenditures.

During 2017, the Churchill Falls (Labrador) Corporation Trust (the Trust) contributed capital in the amount of \$0.2 (2016 - \$0.3 million).

22. CAPITAL MANAGEMENT

Nalcor's principal business requires ongoing access to capital in order to maintain assets and ensure the continuity of its operations as a going concern. Nalcor also requires access to capital to fund its various development activities relating to Oil and Gas and the Lower Churchill Project. Therefore, Nalcor's primary objective when managing capital is to ensure ready access to capital at a reasonable cost, to minimize its cost of capital within the confines of established risk parameters, and to safeguard Nalcor's ability to continue as a going concern.

The capital managed by Nalcor is comprised of debt (long-term debentures, promissory notes, bank credit facilities and Class B limited partnership units) and equity (share capital, shareholder contributions, reserves and retained earnings).

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

A summary of the consolidated capital structure is outlined below:

<i>As at December 31 (millions of Canadian dollars)</i>	2017		2016	
Debt				
Sinking funds (Hydro portion only)	(190)		(267)	
Short-term borrowings	369		435	
Current portion of long-term debt	7		143	
Long-term debt	9,386		5,873	
Class B limited partnership units	491		399	
	10,063	66.4%	6,583	60.7%
Equity				
Share capital	123		123	
Shareholder contributions	3,693		2,861	
Reserves	(71)		7	
Retained earnings	1,336		1,273	
	5,081	33.6%	4,264	39.3%
Total Debt and Equity	15,144	100.0%	10,847	100.0%

Nalcor's committed operating facility has covenants restricting the issuance of debt such that the unconsolidated debt to total capitalization ratio cannot exceed 70.0%. The covenants further stipulate that the debt service coverage ratio should at all times be greater than 1.5 on an unconsolidated basis. As at December 31, 2017, Nalcor was in compliance with these covenants.

22.1 Hydro

Hydro's principal business requires ongoing access to capital in order to maintain assets to ensure the continued delivery of safe and reliable service to its customers. Therefore, Hydro's primary objective when managing capital is to ensure ready access to capital at a reasonable cost, to minimize its cost of capital within the confines of established risk parameters, and to safeguard Hydro's ability to continue as a going concern.

Hydro's approach to capital management encompasses various factors including monitoring the percentage of floating rate debt in the total debt portfolio, the weighted average term to maturity of its overall debt portfolio, its percentage of debt to debt plus equity, and its interest coverage.

For the regulated portion of Hydro's operations, Management targets a capital structure comprised of 75% debt and 25% equity, a ratio which Management believes to be optimal with respect to its cost of capital. This capital structure is maintained by a combination of dividend policy, shareholder contributions and debt issuance. The issuance of any new debt with a term greater than one year requires prior approval of the PUB. Hydro's committed operating facility has a covenant restricting the issuance of debt such that consolidated debt to total capitalization ratio cannot exceed 85%. As at December 31, 2017, Hydro was in compliance with this covenant.

Legislation stipulates that the total of the Government guaranteed short-term loans issued by Hydro and outstanding at any time shall not exceed a limit as fixed by the Lieutenant-Governor in Council. Short-term loans are those loans issued with a term not exceeding two years. The current limit is set at \$300.0 million and \$144.0 million is outstanding as at December 31, 2017 (2016 - \$210.0 million). Issuance of short term borrowings and long-term debt by Hydro is further restricted by Bill C-24, an amendment to the Newfoundland and Labrador Hydro Act of 1975. The Bill effectively limits Hydro's total borrowings, which includes both short term and long-term debt, to \$2.1 billion at any point in time.

Historically, Hydro addressed longer-term capital funding requirements by issuing government guaranteed long-term debt in the domestic capital markets. However, in December 2017, the process changed to one whereby the Province issues debt specifically on Hydro's behalf and lends the proceeds to Hydro. The Province authorized funding up to \$700.0 million, which includes \$225.0 million to repay an outstanding promissory note to the Province through Nalcor, due March 31, 2018. As at December 31, 2017, \$300.0 million of the \$700.0 million authorized has been issued.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

22.2 Oil and Gas

Oil and Gas' objective when managing capital is to maintain its ability to fund operating costs and expenditures related to development and production assets, on a timely basis. Oil and Gas maintains a \$30 million unsecured demand credit facility, which is used to finance operations in the short-term. Long-term capital includes share capital, shareholder contributions and retained earnings. Oil and Gas' future requirements for capital are expected to decline as construction on existing joint venture projects decreases. During this time, it is expected that Oil and Gas' cash flow from operations will be sufficient to fund its capital needs. Additional requirements will be funded through Oil and Gas' credit facility.

22.3 Energy Marketing

Energy Marketing's objective when managing capital is to maintain its ability to continue as a going concern. Energy Marketing's capital consists of shareholders' equity, specifically, share capital, reserves and retained earnings. Capital resource requirements are limited to working capital needs, which are funded through cash from operations, support from its parent, and a \$20.0 million demand operating facility with its primary banker.

22.4 Bull Arm

Bull Arm Fabrication's objective when managing capital is to maintain its ability to continue as a going concern. The focus of the capital management policy is to provide flexibility to ensure cash continues to be available to satisfy capital requirements. In 2013, Bull Arm Fabrication implemented its Board approved dividend policy of paying dividends to Nalcor when, together, cash and short-term investment balances exceed \$1.0 million.

22.5 Churchill Falls

Churchill Falls' objective when managing capital is to maintain its ability to continue as a going concern. Churchill Falls' requirements for capital in the future are expected to remain constant, coincident with the aging of the plant and related infrastructure and the execution of the long-term asset management plan. The focus of the capital management policy is to provide flexibility to ensure cash continues to be available to satisfy capital requirements. Managing the level of common dividend payments is a key aspect of ensuring the availability of funding to maintain the plant and infrastructure.

At present, the capital position of Churchill Falls is comprised entirely of equity capital (issued capital, shareholder contributions, reserves and retained earnings). The capital structure is adjusted through the amount of dividends paid to shareholders.

22.6 Muskrat Falls

The capital structure of Muskrat Falls includes long-term debt, share capital and shareholder contributions. The 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 Muskrat Falls hydroelectric facility. Muskrat Falls' future requirements for capital are expected to increase commensurate with progress on the construction. During this time, it is expected that proceeds from the Muskrat/LTA Construction Facility and shareholder contributions will be sufficient to fund the development of the Muskrat Falls hydroelectric facility. The Province of Newfoundland and Labrador has provided a guarantee of equity support in relation to the construction of the Muskrat Falls hydroelectric facility. These guarantees, together with the proceeds from long-term debt, will ensure sufficient funds are available to finance construction.

22.7 LCP Transmission (LIL LP and Labrador Transco)

The capital structure of the LIL LP is comprised of partner capital (issued units, cash calls and deficit) and long-term debt. The capital structure is adjusted through the amount of distributions paid to the Partners as well as capital contributions.

LIL LP's objective when managing capital is to fund the construction of the LIL while providing its partners a required return. LIL LP's requirements for capital in the future are expected to increase, coincident with the development of the LIL. The focus of the capital management policy is to provide flexibility to ensure cash continues to be available to satisfy capital requirements. Managing cash calls from the limited partners is a key aspect of ensuring the availability of funding to develop the LIL. The Province of Newfoundland and Labrador have provided guarantees of partner contributions in relation to the construction of the LIL. These partner contributions, together with the proceeds from long-term debt, will be sufficient to fund the development and construction of the LIL.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

The capital structure of Labrador Transco includes long-term debt, share capital and shareholder contributions. The objectives for managing capital are to maintain its ability to continue as a going concern and to ensure timely payment of its contractual obligations as they relate to the construction of the LTA. It is expected that proceeds from the Muskrat/LTA Construction Facility and shareholder contributions will be sufficient to fund the development of the LTA. The Province of Newfoundland and Labrador has provided guarantees of equity support in relation to the construction of the LTA. These guarantees, together with the proceeds from long-term debt will ensure sufficient funds are available to finance construction.

23. REVENUE

<i>For the year ended December 31 (millions of Canadian dollars)</i>	2017	2016
Electricity sales	616	624
GWAC revenue	24	24
Petroleum and natural gas sales	228	137
Royalty expense	(10)	(6)
Total energy sales	858	779
Lease revenue	49	21
Government funding	1	2
Preferred dividends	2	4
Other	20	18
Total other revenue	72	45

24. OPERATING COSTS

<i>For the year ended December 31 (millions of Canadian dollars)</i>	2017	2016
Salaries and benefits	135	130
Maintenance and materials	39	35
Professional services	15	18
Advertising, donations and community involvement	10	1
Insurance	7	6
Travel and transportation	7	6
Rental and royalty	4	5
Other operating costs	2	6
	219	207

25. PRODUCTION, MARKETING AND TRANSPORTATION COSTS

Production, marketing and transportation costs include costs incurred related to the operating, processing and transportation of oil.

<i>For the year ended December 31 (millions of Canadian dollars)</i>	2017	2016
Project operating costs	22	16
Processing and marketing	9	6
Transportation and transshipment	5	4
	36	26

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

26. TRANSMISSION RENTAL AND MARKET FEES

Transmission rental and market fees are related to the sale and transmission of energy to export markets.

<i>For the year ended December 31 (millions of Canadian dollars)</i>	2017	2016
Transmission rental	24	21
Market fees	1	1
	25	22

27. NET FINANCE EXPENSE

<i>For the year ended December 31 (millions of Canadian dollars)</i>	2017	2016
Finance income		
Interest on sinking fund	13	15
Interest on reserve fund	-	1
Interest on investments	13	8
Interest on restricted cash	14	15
Other interest income	5	2
	45	41
Finance expense		
Long-term debt	314	273
Class B limited partnership units	37	24
Debt guarantee fees	13	4
Accretion	7	7
Other	8	3
	379	311
Interest capitalized during construction	(268)	(198)
	111	113
Net finance expense	66	72

The effective interest rate on short-term investments at December 31, 2017 was 1.52% per annum (2016 - 1.00%).

28. OTHER EXPENSE (INCOME)

<i>For the year ended December 31 (millions of Canadian dollars)</i>	2017	2016
Settlement of commodity swaps	2	(10)
Settlement of foreign exchange forward contracts	(1)	-
Financial transmission rights income and amortization	(1)	(2)
Cash flow hedge ineffectiveness	1	-
Loss on disposal of property, plant and equipment	20	7
Asset disposal costs	-	1
Unrealized foreign exchange loss	-	1
Realized foreign exchange loss	3	-
Other	(1)	(1)
Other expense (income)	23	(4)

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

29. ACCUMULATED OTHER COMPREHENSIVE LOSS

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

Items that may or have been reclassified to profit or loss:

<i>(millions of Canadian dollars)</i>	2017	2016
Employee future benefits		
Balance at January 1	(27)	(27)
Net actuarial loss on defined benefit plans	(3)	-
Balance at December 31	(30)	(27)
<i>(millions of Canadian dollars)</i>	2017	2016
Available-for-sale financial instruments		
Balance at January 1	48	45
Fair value (loss) gain during the year	(2)	13
Amounts reclassified to profit or loss	(8)	(10)
Balance at December 31	38	48
<i>(millions of Canadian dollars)</i>	2017	2016
Cash flow hedges		
Balance at January 1	(14)	(6)
Fair value loss during the year	(66)	(2)
Amounts reclassified to profit or loss	1	(6)
Balance at December 31	(79)	(14)

30. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

30.1 Fair Value

The estimated fair values of financial instruments as at December 31, 2017 and December 31, 2016 are based on relevant market prices and information available at the time. Fair value estimates are based on valuation techniques which are significantly affected by the assumptions used including the amount and timing of future cash flows and discount rates reflecting various degrees of risk. As such, the fair value estimates below are not necessarily indicative of the amounts that Nalcor might receive or incur in actual market transactions.

As a significant number of Nalcor'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 Nalcor 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, Nalcor determines whether transfers have occurred between

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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 for the years ended December 31, 2017 and December 31, 2016.

<i>As at (millions of Canadian dollars)</i>	Level	Category	Carrying Value December 31, 2017	Fair Value December 31, 2017	Carrying Value December 31, 2016	Fair Value December 31, 2016
Financial assets						
Derivative assets	2,3	FVTPL ¹	3	3	1	1
Sinking funds - investments in Hydro debt issue	2	HTM ²	45	56	57	71
Sinking funds - other investments	2	AFS ³	231	231	307	307
Long-term investments	1,2	HTM ²	332	332	34	34
Reserve fund	2	AFS ³	-	-	15	15
Long-term receivables	2	L&R ⁴	-	-	28	28
Financial liabilities						
Derivative liabilities	2	FVTPL ¹	8	8	5	5
Long-term debt including amount due within one year (before sinking funds)	2	OFL ⁵	9,438	10,500	6,073	6,965
Class B limited partnership units	3	OFL ⁵	491	491	399	399
Long-term payables	2	OFL ⁵	52	56	58	75

1. Fair value through profit or loss
2. Held-to-maturity investments
3. Available-for-sale financial assets
4. Loans and receivables
5. Other financial liabilities

The fair value of cash and cash equivalents, restricted cash, short-term investments, trade and other receivables, short-term borrowings and trade and other payables approximates 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 derivative instruments are valued based on observable commodity future curves, broker quotes or other publicly available data. Level 2 fair values of other risk management assets and liabilities and long-term debt are determined using observable inputs other than unadjusted quoted prices, such as interest rate yield curves and currency rates.

Level 3 financial instruments include financial transmission rights and Class B limited partnership units.

Financial transmission rights are purchased contracts used to mitigate risk associated with congestion in export markets. The following table summarizes quantitative information about the valuation techniques and unobservable inputs used in the fair value measurement of financial transmission rights as at December 31, 2017.

<i>(millions of Canadian dollars)</i>	Carrying Value	Valuation Techniques	Significant Unobservable Input(s)	Range
Derivative assets (Financial transmission rights)	0.3	Modelled pricing	Price, seasonality and market factors	-10% to 2%

Methodologies for calculating the fair values of financial transmission rights are determined by using underlying contractual data as well as observable and unobservable inputs. Fair value methodologies are reviewed by Management on a quarterly basis to assess the reasonability of the assumptions made and models are adjusted as necessary for significant expected changes in fair

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

value due to changes in key inputs. As at December 31, 2017, the effect of using reasonably possible alternative assumptions regarding the unobservable implied volatilities may have resulted in -\$32,900 to \$7,700 change in the carrying value of the financial transmission rights.

The Class B limited partnership units are carried at amortized cost calculated using the effective interest method. The effective interest rate of 8.5% (2016 – 8.8%) is defined in the Newfoundland and Labrador Development Agreement as Emera NL's rate of return on equity (RROE), and is equal to the rate approved by the PUB for privately-owned regulated electrical utilities. Due to the unobservable nature of the effective interest rate and cash flows associated with the units, the fair value is assumed to approximate carrying value and the instruments have therefore been classified as Level 3.

The table below sets forth a summary of changes in fair value of the Class B limited partnership units given a one percent change in the discount rate while holding other variables constant:

<i>(millions of Canadian dollars)</i>	1% Increase	1% Decrease
Class B limited partnership units	(10.5)	10.3

30.2 Risk Management

Nalcor 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 Nalcor's expected future cash flows.

Credit Risk

Nalcor's expected future cash flows are exposed to credit risk through its operating activities, primarily due to the potential for non-performance by its customers, and through its financing and investing activities, based on the risk of non-performance by counterparties to its financial instruments. The degree of exposure to credit risk on cash and cash equivalents, short-term investments, long-term investments and derivative assets as well as from the sale of electricity to customers, including the associated accounts receivable, is determined by the financial capacity and stability of those customers and counterparties. The maximum exposure to credit risk on these financial instruments is represented by their carrying values on the Consolidated Statement of Financial Position at the reporting date.

Credit risk on cash and cash equivalents is considered to be minimal, as Nalcor's cash deposits are held by a Schedule 1 Canadian Chartered bank with a rating of A+ (Standard and Poor's). Credit risk on restricted cash is considered to be minimal, as Nalcor's restricted cash deposits are held by Schedule 1 Canadian Chartered banks with a rating of AA- (Standard and Poor's). Credit risk on short-term investments is minimized by limiting holdings to high-quality, investment grade securities issued by the Federal and Provincial governments, as well as BAs and term deposits issued by Schedule 1 Canadian Chartered banks.

Credit exposure on Nalcor's sinking funds is limited by restricting the holdings to long-term debt instruments issued by the Government of Canada or any province of Canada, Crown corporations and Schedule 1 Canadian Chartered banks. The following credit risk table provides information on credit exposures according to issuer type and credit rating for the remainder of the sinking fund's portfolio:

	Issuer Credit Rating	Fair Value of Portfolio (%)	Issuer Credit Rating	Fair Value of Portfolio (%)
	2017		2016	
Provincial governments	AA- to AAA	-	AA- to AAA	0.37%
Provincial governments	A- to A+	46.14%	A- to A+	44.29%
Provincially owned utilities	A- to A+	53.86%	A- to A+	49.22%
Schedule 1 Canadian banks	A- to A+	-	A- to A+	6.12%
		100.00%		100.00%

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Credit exposure on the reserve fund is mitigated by adhering to an investment policy which restricts the holdings to long-term debt instruments issued or guaranteed by the Government of Canada or any province of Canada. Investments in the long-term debt instruments of Canadian banks are also permitted, provided the bank is rated A or higher by Standard and Poor's. With the exception of the Government of Canada, holdings of any one issuer are limited to 10.0% of the total principal amount of the portfolio. The following credit risk table provides information on credit exposures according to issuer type and credit rating for the reserve fund:

	Issuer Credit Rating	Fair Value of Portfolio (%)	Issuer Credit Rating	Fair Value of Portfolio (%)
	2017		2016	
Provincial governments	AA- to AAA	-	AA- to AAA	7.32%
Provincial governments	A- to A+	-	A- to A+	30.63%
Schedule 1 Canadian banks	AA- to AAA	-	AA- to AAA	9.07%
Schedule 1 or 2 Canadian banks	A- to A+	-	A- to A+	52.98%
		-		100.00%

As at December 31, 2017, the reserve fund balance was fully withdrawn.

Credit exposure on Nalcor's long-term investments is considered to be limited as the investments are held by Schedule 1 Canadian Chartered banks and Provincially owned utilities investment grade ratings of A- or higher (Standard and Poor's). The following credit risk table provides information on credit exposures according to issuer type and credit rating for the long-term investments:

	Issuer Credit Rating	Fair Value of Portfolio (%)	Issuer Credit Rating	Fair Value of Portfolio (%)
	2017		2016	
Provincially owned utilities	A- to A+	0.01%	A- to A+	0.08%
Schedule 1 Canadian Banks	AA- to AAA	-	AA- to AAA	72.65%
Schedule 1 Canadian Banks	A- to A+	99.99%	A- to A+	27.27%
		100.00%		100.00%

Credit exposure on derivative assets is limited by a Financial Risk Management Policy as approved by the Board, which restricts available counterparties for hedge transactions to Schedule 1 Canadian Chartered banks and Federally Chartered US banks.

Nalcor does not have any significant amounts that are past due and uncollectable, for which a provision has not been recognized at December 31, 2017.

Liquidity Risk

Nalcor is exposed to liquidity risk with respect to its contractual obligations and financial liabilities, including any derivative liabilities related to hedging activities. Liquidity risk management is aimed at ensuring cash is available to meet those obligations as they become due.

Short-term liquidity for Nalcor and its subsidiaries is mainly provided through cash and cash equivalents on hand, funds from operations, an operating credit facility which Nalcor maintains with its banker, and shareholder contributions. Nalcor maintains a \$250.0 million (2016 - \$250.0 million) committed revolving term credit facility, with a maturity date of January 31, 2019. There were no amounts drawn on this facility at December 31, 2017 (2016 - \$nil). In addition, Hydro has access to a \$300.0 million promissory note program and a \$200.0 million (2016 - \$50.0 million) revolving term credit facility. Oil and Gas and Churchill Falls also maintain demand operating facilities of \$30.0 million (2016 - \$30.0 million) and \$10.0 million (2016 - \$10.0 million), respectively. Churchill Falls maintains a \$23.0 million minimum cash balance (2016 - \$22.0 million). Energy Marketing maintains a demand operating facility of \$20.0 million (2016 - \$20.0 million).

Liquidity risk for Muskrat Falls and Labrador Transco is considered to be minimal, as both companies can access the funds drawn down from the MF/LTA construction facility for the payment of construction costs as well as interest payments. The LIL LP has

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

access to the funds drawn down from the LIL construction facility for the payment of construction costs as well as interest payments.

Long-term liquidity risk for Hydro is managed by the issuance of a portfolio of debt with maturity dates ranging from 2026 to 2048. Sinking funds have been established for these issues, with the exception of the issues maturing in 2045 and 2048. For Churchill Falls, long-term liquidity risk is managed by maintenance of the reserve fund in accordance with the Shareholders' Agreement and a dividend management policy that meets long-term liquidity requirements associated with Churchill Falls' capital expenditure program.

The following are contractual maturities of Nalcor's financial liabilities, including principal and interest as at December 31, 2017:

<i>(millions of Canadian dollars)</i>	< 1 Year	1-3 Years	3-5 Years	> 5 Years	Total
Trade and other payables	584	-	-	-	584
Short-term borrowings	369	-	-	-	369
Derivative liabilities	8	-	-	-	8
Long-term debt (including sinking funds)	353	801	1,083	15,272	17,509
Class B partnership units	-	-	162	2,666	2,828
Long-term payables	9	20	10	58	97
	1,323	821	1,255	17,996	21,395

Market Risk

In the course of carrying out its operating, financing and investing activities, Nalcor is exposed to possible market price movements that could impact expected future cash flow and the carrying value of certain financial assets and liabilities. Market price movements to which Nalcor has significant exposure include those relating to prevailing interest rates, foreign exchange rates, most notably USD/CAD, and current commodity prices, most notably the spot prices for diesel fuel, electricity, No. 6 fuel and oil. These exposures are addressed as part of the Financial Risk Management Strategy.

Interest Rates

Changes in prevailing interest rates will impact the fair value of financial assets and liabilities classified as held for trading or available-for-sale, which includes Nalcor's short-term investments, sinking funds and reserve fund. Expected future cash flows associated with those financial instruments can also be impacted. The impact of a 0.5% change in interest rates on the Consolidated Statement of Profit and Comprehensive (Loss) Income associated with cash and cash equivalents and short-term investments was immaterial throughout 2017 due to the short time period to maturity.

The table below shows the impact of a 0.5% change in interest rates on other comprehensive (loss) income associated with the sinking funds as at December 31, 2017:

<i>(millions of Canadian dollars)</i>	0.5% Decrease	0.5% Increase
Interest on sinking funds	12.0	(11.3)

The impact of interest rates on the expected future cash outflows related to short-term borrowings (which includes promissory notes and BAs issued under Nalcor's credit lines) and long-term debt are managed within the corporate financing strategy whereby floating rate debt exposures and interest rate scenarios are forecasted and evaluated. A diversified portfolio of fixed and floating rate debt is maintained and managed with a view to an acceptable risk profile. Key quantitative parameters for interest rate risk management includes the percentage of floating rate debt in the total debt portfolio, coupled with an examination of the weighted average term to maturity of the entire debt portfolio. By setting clear guidelines in respect to these quantitative parameters, Nalcor attempts to minimize the likelihood of a material impact on profit or loss resulting from an unexpected change in interest rates.

In May 2017, Muskrat Falls, jointly with Labrador Transco, entered into six bond forward contracts 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

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

relationship and the resulting change in fair value of \$65.9 million was recorded in other comprehensive (loss) income with the ineffective portion of \$1.1 million recognized immediately in other expense (income). The amortization of the other comprehensive (loss) income 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 hydroelectric facility and LTA 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 as at December 31, 2017 including the previous cash flow hedge initiated in December 2013 was \$1.8 million (2016 - \$0.8 million).

Foreign Currency and Commodity Exposure

Nalcor's primary exposure to both foreign exchange and commodity price risk arises from its purchases of No. 6 fuel for consumption at the HTGS, capital purchases, USD denominated electricity sales, rental revenues and the sale of crude oil. For the purchase of No.6 fuel, these risks are mitigated through the operation of the RSP. Exposures to USD denominated electricity sales are addressed in accordance with the Board-approved Financial Risk Management Policy. Tactics include the use of forward rate agreements and fixed price commodity swaps.

The table below shows the impact of a 0.5% change in foreign exchange rates on trade and other payables as at December 31, 2017:

<i>(millions of Canadian dollars)</i>	0.5% Decrease	0.5% Increase
Trade and other payables	(2.0)	2.0

During 2017, total energy sales denominated in USD were \$35.3 million (2016 - \$31.7 million). To mitigate foreign exchange risk on these sales, Energy Marketing used foreign currency forward contracts. In December 2016, Energy Marketing entered into a series of foreign exchange forward contracts with a notional value of \$20.2 million USD and an average exchange rate of \$1.32 CAD per USD to hedge foreign exchange risk on 58% of planned USD energy sales for 2017.

In November 2017, Energy Marketing entered into a series of foreign exchange forward contracts with a notional value of \$9.7 million USD on 36% of 2018 budgeted USD sales at an average rate of \$1.28 CAD per USD.

As the foreign exchange forward contracts have been designated as hedging instruments, changes in fair value have been recorded in other comprehensive (loss) income. During 2017, \$0.4 million in gains from foreign exchange forward contracts were included in other expense (income) (2016 - \$0.1 million losses) and \$0.2 million in gains (2016 - \$0.3 million in losses) remain in other comprehensive (loss) income.

Also, in November 2017, Energy Marketing entered into commodity contracts with a notional value of \$4.4 million USD on 11% of 2018 budgeted Recapture volume at an average rate of \$43.84 USD/MWh. These commodity contracts were entered into to mitigate price fluctuations on export market sales.

The commodity contracts have also been designated as hedging instruments and at December 31, 2017, \$1.3 million in unrealized losses have been recorded in other comprehensive (loss) income (2016 - \$nil).

During 2017, additional financial transmission rights with notional values of \$0.9 million USD were purchased to mitigate risk on congestion for the remainder of 2017 and a significant portion of 2018. As the rights have not been designated as hedging instruments, changes in fair value have been recorded in other expense (income).

During 2017, total oil sales denominated in USD were \$168.6 million (2016 - \$93.6 million). While Oil and Gas has exposure to fluctuations in the USD/CAD exchange rate on those sales, a significant portion of Oil and Gas' planned capital expenditures for 2017 were denominated in USD, which mitigated this exposure.

On November 30, 2016, Oil and Gas entered into a series of commodity price swap contracts to hedge commodity price risk on approximately 25% of anticipated 2017 production. These contracts had a notional value of \$32.3 million USD and an average

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

fixed price of \$52.09 USD per barrel. During 2017, \$1.9 million in realized losses (2016 - \$6.2 million in gains) from commodity price swaps contracts, designated under hedge accounting, were included in other expense (income). As these contracts have been designated as hedging instruments, changes in fair value have been recorded in other comprehensive (loss) income.

In December 2016, Oil and Gas entered into series of foreign exchange forward contracts to hedge foreign exchange risk on approximately 23% of anticipated USD oil sales in 2017. These contracts had a notional value of \$32.3 million USD and an average fixed rate of \$1.33 CAD per USD. During 2017, \$0.7 million in realized gains from foreign exchange forward contracts, designated under hedge accounting, were included in other expense (income). As these contracts have been designated as hedging instruments, changes in fair value have been recorded in other comprehensive (loss) income.

On November 27, 2017, Oil and Gas entered into a series of commodity price swaps to hedge commodity price risk on approximately 50% of anticipated 2018 production. These contracts have a notional value of \$97.9 million USD, and provide an average fixed price of \$61.36 USD per barrel.

On November 28, 2017 Oil and Gas entered into series of foreign exchange forward contracts to hedge foreign exchange risk on USD oil sales in 2018. These contracts have a notional value of \$97.9 million USD, and an average fixed rate of \$1.28 CAD per USD. Combined with one remaining contract already in place, Oil and Gas have hedged \$100.6 million in USD energy sales at an average fixed rate of \$1.28 CAD per USD.

As these contracts have been designated as hedging instruments, changes in fair value have been recorded in other comprehensive (loss) income. For the year ended December 31, 2017, \$4.6 million in losses (2016 - \$4.8 million in losses) remain in other comprehensive (loss) income.

During 2017, total rental revenue denominated in USD was \$36.6 million (2016 - \$16.1 million). In December 2016, Bull Arm entered into a series of foreign exchange contracts with a total notional value of \$16.1 million USD and a weighted average fixed exchange rate of \$1.32 CAD per USD. Combined with hedge contracts previously entered into during 2015, 100% of budgeted USD revenue for 2017 and the first two months of 2018 was hedged at a weighted average fixed change rate of \$1.32 CAD per USD.

As at December 31, 2017, Bull Arm Fabrication had no remaining foreign exchange forward contracts. The contracts for January and February 2018, with a notional value of \$2.7 million USD and a weighted average fixed exchange rate of \$1.32 CAD per USD, were settled in December 2017 as the sublease concluded during the month. As these contracts were all designated as hedging instruments, changes in fair value were recorded in other comprehensive (loss) income. For the year ended December 31, 2017, \$0.4 million in gains (2016 - \$0.2 million in losses) have been included in other expense (income) related to the forward contracts. As at December 31, 2017, there are no derivative instruments remaining.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

The components of change impacting the carrying value of derivative assets and liabilities for the years ended December 31, 2017 and 2016 are as follows:

	Commodity and forward contracts		Other derivatives		Total
	Level II	Level II	Level III	Level II	Level III
<i>(millions of Canadian dollars)</i>					
Balance at January 1, 2017	(5)	-	1	(5)	1
Purchases	-	-	1	-	1
	(5)	-	2	(5)	2
Changes to profit					
Amortization	-	-	(2)	-	(2)
Total	-	-	(2)	-	(2)
Changes in other comprehensive loss					
Mark-to-market	-	-	-	-	-
Settlements realized in profit or loss	-	-	-	-	-
Total	-	-	-	-	-
Balance at December 31, 2017	(5)	-	-	(5)	-
Balance at January 1, 2016	2	2	-	4	-
Purchases	-	-	2	-	2
	2	2	2	4	2
Changes to profit					
Amortization	-	-	(1)	-	(1)
Mark-to-market	4	-	-	4	-
Settlements	(1)	(2)	-	(3)	-
Total	3	(2)	(1)	1	(1)
Changes in other comprehensive loss					
Mark-to-market	(3)	-	-	(3)	-
Settlements realized in profit or loss	(7)	-	-	(7)	-
Total	(10)	-	-	(10)	-
Balance at December 31, 2016	(5)	-	1	(5)	1

31. RELATED PARTY TRANSACTIONS

Nalcor enters into various transactions with its shareholder and other affiliates. These transactions occur within 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 Nalcor transacts are as follows:

Related Party	Relationship
The Province	100% shareholder of Nalcor
Churchill Falls	Joint arrangement of Hydro
Hydro-Québec	34.2% shareholder of Churchill Falls
Twin Falls	Joint venture of Churchill Falls
Churchill Falls (Labrador) Corporation Trust (The Trust)	Created by the Province with Churchill Falls as the beneficiary
LIL LP	Partnership in which Nalcor holds 75 Class A Partnership Units, 1 Class C Partnership Unit and 1 General Partner Unit
PUB	Agency of the Province

Routine operating transactions with related parties are settled at prevailing market prices under normal trade terms. Outstanding balances due to or from related parties are non-interest bearing with no set terms of repayment, unless otherwise stated.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

- (a) Hydro is required to incur the costs of operations, hearings and application costs of the PUB, including costs of any experts and consultants engaged by the PUB. During 2017, Hydro incurred \$1.8 million (2016 - \$1.3 million) in costs related to the PUB and has included \$3.0 million (2016 - \$2.1 million) in trade and other payables.
- (b) The Hydro debt guarantee fee for 2017 was \$4.1 million (2016 - \$4.5 million). It was paid to the Province on March 27, 2017.
- (c) For the year ended December 31, 2017, Hydro has purchased \$26.3 million (2016 - \$25.2 million) of power generated from assets related to Exploits Generation, which are held by the Province.
- (d) Hydro recorded \$nil (2016 - \$0.2 million) as a rate subsidy for rural isolated customers from the Province and \$1.8 million (2016 - \$1.8 million) as an energy rebate to offset the cost of basic electricity consumption for Labrador rural isolated residential customers under the Northern Strategic Plan. As at December 31, 2017, there is a balance of \$0.6 million (2016 - \$1.3 million) outstanding in trade and other receivables.
- (e) During 2017, Churchill Falls generated revenue from Hydro-Québec of \$94.6 million (2016 - \$102.4 million) and Nalcor has recognized its share of \$62.2 million (2016 - \$67.4 million).
- (f) Under the terms of the Churchill Falls (Labrador) Corporation Limited (Lease) Act, 1961 (the Lease) and amendments thereto, Churchill Falls is required to pay the Province an annual rental of 8% of the consolidated net profits before income taxes and an annual royalty of \$0.50 per horsepower year generated, as defined in the Lease. At December 31, 2017, \$6.4 million (2016 - \$7.5 million) was payable to the Province. Nalcor has recognized its share of \$4.2 million (2016 - \$4.9 million).
- (g) In February 3, 2010, the Province established the Trust with Churchill Falls as the beneficiary. The purpose of the Trust is to fund the external costs and expenses incurred in relation to the motion filed by Churchill Falls seeking a modification to the pricing terms of the 1969 Power Contract. To date, \$5.6 million (2016 - \$5.3 million) has been received and \$nil (2016 - \$13.0 thousand) has been accrued as receivable from the Trust. Nalcor has recognized its share of \$3.7 million (2016 - \$3.5 million) as received and \$nil (2016 - \$8.6 thousand) accrued as receivable from the Trust.
- (h) As at December 31, 2017, Churchill Falls capacity penalty payable was \$0.4 million (2016 - \$0.4 million), of which Nalcor has recorded its share of \$0.3 million (2016 - \$0.3 million). The capacity penalty relates to the supply of power to Hydro-Québec. Churchill Falls did not incur a capacity penalty in 2017 (2016 - \$nil).
- (i) For the year ended December 31, 2017, Oil and Gas expensed \$10.3 million (2016 - \$6.4 million) to the Province for royalties on its oil and gas operations.
- (j) On December 20, 2017, Hydro issued new long-term debt, Series 1A, with face value of \$300.0 million. The Province of Newfoundland and Labrador issued debt specifically on Hydro's behalf and lent the proceeds to Hydro.

31.1 Key Management Personnel

Compensation for key management personnel, which Nalcor defines as its executives who have the primary authority and responsibility in planning, directing and controlling the activities of the entity, includes compensation for senior executives. Salaries and employee benefits include base salaries, performance contract payments, vehicle allowances and contributions to employee benefit plans. Post-employment benefits include contributions to the Province's Public Service Pension Plan.

<i>For the year ended December 31 (millions of Canadian dollars)</i>	2017	2016
Salaries and employee benefits*	6	10
Post-employment benefits	-	1
	6	11

*2016 includes severance and related costs incurred in the second quarter.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

32. COMMITMENTS AND CONTINGENCIES

- (a) Nalcor and its subsidiaries have received claims instituted by various companies and individuals with respect to power delivery claims and other miscellaneous matters. Although the outcome of such matters cannot be predicted with certainty, Management believes Nalcor's exposure to such claims and litigation, to the extent not covered by insurance or otherwise provided for, is not expected to materially affect its financial position or results of operations.
- (b) Outstanding commitments for capital projects, excluding those related to Oil and Gas, total approximately \$1.0 billion as at December 31, 2017 (December 31, 2016 - \$2.1 billion). Prefunded equity requirements associated with Project Finance Agreements in Muskrat Falls and LCP Transmission total approximately \$1.0 billion as at December 31, 2017 (December 31, 2016 - \$2.8 billion).
- (c) Nalcor and its subsidiaries have issued 20 irrevocable letters of credit with a total value of \$41.7 million as per Note 14.1.
- (d) LCP has the following sinking fund instalments due for the next five years:

<i>(millions of Canadian dollars)</i>	2018	2019	2020	2021	2022
Sinking fund instalments	-	-	64.0	128.0	128.0

- (e) Oil and Gas has the following commitments as a result of its joint venture partnerships:

<i>(millions of Canadian dollars)</i>	Operating	Capital	Total Commitments
2018	15.9	7.2	23.1
2019	9.3	-	9.3
2020	9.3	-	9.3
2021	8.7	-	8.7
2022	8.5	-	8.5
Thereafter	6.3	-	6.3

- (f) Hydro has entered into a number of long-term power purchase agreements as follows:

Type	Rating	Effective Date	Term
Hydroelectric	3 MW	1995	25 years
Hydroelectric	4 MW	1998	25 years
Cogeneration	15 MW	2003	20 years
Wind	390 MW	2004	15 years
Wind	27 MW	2008	20 years
Wind	27 MW	2009	20 years
Wind	300 kW	2010	Continual
Hydroelectric	175 kW	2017	15 years

Estimated payments due in each of the next five years are as follows:

<i>(millions of Canadian dollars)</i>	2018	2019	2020	2021	2022
Power purchases	30.7	31.9	32.5	32.6	32.7

- (g) In 2014, Hydro entered into three Capacity Assistance Agreements, one with Vale Newfoundland & Labrador Limited (Vale) and two with Corner Brook Pulp and Paper Limited (CBPP) for the purchase of relief power during the winter period. In 2016, Hydro also entered into two new Capacity Assistance Agreements, one with Praxair and a second agreement with Vale for the purchase of relief power. The agreements with Vale and Praxair have a supply period defined as December 1 to March 31 for each contract year, concluding March 2018. In November 2017, Hydro entered into a revised agreement with CBPP that

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

expires the earlier of April 30, 2022 or the commissioning of the Muskrat Falls plant. Payment for services will be dependent on the successful provision of capacity assistance for the winter period by Vale, CBPP and Praxair.

- (h) Energy Marketing holds firm transmission rights with a number of counterparties in order to gain access to export markets. As at December 31, 2017, commitments for transmission rights total \$22.6 million for 2018. No transmission rights held by Energy Marketing extend beyond 2019.
- (i) 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.
- (j) As part of the MF/LTA PFA, Muskrat Falls and Labrador Transco have pledged its present and future assets as security to the Collateral Agent.
- (k) Under the terms of the Newfoundland and Labrador Development Agreement (NLDA), LIL GP has certain responsibilities and provisions of duty with which it must comply in its role as the general partner. Any failure of LIL GP to comply with the NLDA will result in Nalcor indemnifying Emera NL for any losses sustained.
- (l) 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 which will commence in 2020.
- (m) On November 29, 2017, Nalcor signed a CDA with the NunatuKavut Community Council, which came into effect December 1, 2017. The CDA is a six year agreement which provides tangible benefits to South Inuit and communities throughout NunatuKavut. Under the CDA there are contingent liabilities with an estimated value of \$1.1 million.
- (n) Under the IBA, Nalcor is required to make implementation payments to the Innu Nation that commenced upon sanction of the Muskrat Falls hydroelectric plant of \$5 million annually escalating by an annual consumer price index. Post first commercial power, when Nalcor begins earning revenue from the sale and delivery of capacity and energy from the facility, Nalcor is required to continue to make annual payments of the greater of \$5 million escalating by an annual consumer price index and 5% of after debt net cash flow, as defined by the agreement.

33. SUPPLEMENTARY CASH FLOW INFORMATION

<i>For the year ended December 31 (millions of Canadian dollars)</i>	2017	2016
Trade and other receivables	(101)	(23)
Prepayments	(2)	4
Inventories	(23)	(15)
Trade and other payables	(578)	165
Changes in non-cash working capital balances	(704)	131
Related to:		
Operating activities	(81)	(46)
Investing activities	(623)	177
	(704)	131

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

34. SEGMENT INFORMATION

The operating structure as at December 31, 2017 reflects organizational changes that resulted in revised operating segments effective January 1, 2017. The designation of segments is based on a combination of regulatory status and management accountability. Previously reported segmented information has been presented to conform with the current operating structure. The following summary provides a brief overview of the nature of the operations included in each of the Company's six business segments.

Hydro - is comprised of both regulated and non-regulated activities.

- **Hydro Regulated** activities encompass sales of electricity to customers within the Province that are regulated by the Newfoundland and Labrador Board of Commissioners of Public Utilities (PUB).
- **Hydro Non-Regulated** activities include the sale of power, purchased from Churchill Falls, to mining operations in Labrador West as well as costs related to operations that Hydro manages that are not subject to rate regulation by the PUB.

Power Development - includes the development activities of the 824 MW **Muskrat Falls** hydroelectric generating facility currently under construction in Labrador on the Lower Churchill River. Once construction is complete this asset and its operating results will become part of the Power Supply segment.

Power Supply - is comprised of the following:

- **LCP Transmission** includes the construction and operation of the LIL and LTA, which consists of transmission lines connecting the Muskrat Falls hydroelectric plant, the Churchill Falls hydroelectric facility, and certain portions of the transmission system in Labrador to the island of Newfoundland.
- **Churchill Falls** owns and operates a hydroelectric generating facility which sells electricity to Hydro-Québec and Hydro.
- **Other** includes revenues and costs recovered from Hydro-Québec associated with Nalcor's operation of the Menihek Generating Station, the Maritime Link (which is owned by Emera, but consolidated by Nalcor), administration and community development costs related to Power Supply, and costs associated with the management of LCP construction.

Energy Markets - includes energy trading activities and commercial activities related to the development of energy markets.

- **Energy Trading** includes the sale of available excess energy, primarily Recapture, to export markets in eastern Canada and the northeastern United States. Recapture refers to excess energy from the 300 MW block of electricity which Churchill Falls has agreed to sell and deliver to Hydro to service its residential, commercial and industrial Labrador Interconnected customers.
- **Commercial and Other** includes costs associated with Gull Island and business development activities related to exploring additional markets and sources for future energy generation and transmission.

Offshore Development - includes the following:

- **Oil and Gas** activities include Nalcor's share of exploration, development, production, transportation and processing sectors of the oil and gas industry.
- **Bull Arm Fabrication** consists of an industrial fabrication site which is subleased to third parties.

Corporate - includes corporate support and shared services functions.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

	Hydro		Power Development	Power Supply			Energy Markets		Offshore Development			Inter-Segment	Total
	Regulated	Non-Regulated	Muskkrat Falls	LCP Transmission	Churchill Falls	Other	Energy Trading	Commercial and Other	Oil and Gas	Bull Arm	Corporate		
<i>(millions of Canadian dollars)</i>													
For the year ended December 31, 2017													
Energy sales	506	40	-	-	91	-	47	-	217	-	-	(43)	858
Other revenue	5	-	-	-	1	9	1	-	7	48	-	1	72
Revenue	511	40	-	-	92	9	48	-	224	48	-	(42)	930
Fuels	226	-	-	-	-	-	-	-	-	-	-	-	226
Power purchased	62	39	-	-	-	-	4	-	-	-	-	(43)	62
Operating costs	130	1	1	3	44	13	5	1	8	1	12	-	219
Production, marketing and transportation costs	-	-	-	-	-	-	-	-	36	-	-	-	36
Transmission rental and market fees	-	-	-	-	-	-	25	-	-	-	-	-	25
Depreciation, depletion, amortization and impairment****	78	-	-	-	18	-	-	51	152	-	1	-	300
Exploration and evaluation	-	-	-	-	-	-	-	-	1	-	-	-	1
Net finance expense (income)	65	-	-	(2)	(1)	-	-	-	3	-	1	-	66
Other expense (income)	6	-	1	-	-	-	(1)	-	15	-	1	1	23
Preferred dividends	-	-	-	-	(2)	-	-	-	-	-	-	2	-
Expenses	567	40	2	1	59	13	33	52	215	1	15	(40)	958
(Loss) profit before regulatory adjustments	(56)	-	(2)	(1)	33	(4)	15	(52)	9	47	(15)	(2)	(28)
Regulatory adjustments	(92)	-	-	-	-	-	-	-	-	-	-	1	(91)
Profit (loss) for the year	36	-	(2)	(1)	33	(4)	15	(52)	9	47	(15)	(3)	63
Capital expenditures*	344	-	1,137	1,140	46	593	-	1	161	-	4	(2)	3,424
Total assets**	2,605	48	5,679	5,841	592	1,773	23	144	1,246	2	406	(325)	18,034
Total debt***	1,668	-	3,606	4,789	-	-	-	-	-	-	-	-	10,063

*Capital expenditures (inclusive of property, plant and equipment and intangible assets) include non-cash additions of \$588.4 million related to the Maritime Link and \$37.2 million related to Class B Limited Partnership Unit accrued interest.

**Total assets include \$1,734.9 million related to the Maritime Link and \$82.0 million related to Class B Limited Partnership Unit accrued interest.

***Total debt includes short-term borrowings, long-term debt including current portion less Hydro's sinking funds of \$190.2 million, and Class B Limited Partnership Units.

****Included in depreciation, depletion, amortization and impairment is an impairment expense of \$50.6 million in Commercial and Other related to the Gull Island Project in addition to an impairment expense of \$81.0 million in Oil and Gas related to seismic and geoscientific data acquisition costs.

NALCOR ENERGY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

	Hydro		Power Development	Power Supply			Energy Markets		Offshore Development		Corporate	Inter-Segment	Total
	Regulated	Non-Regulated	Muskrat Falls	LCP Transmission	Churchill Falls	Other	Energy Trading	Commercial and Other	Oil and Gas	Bull Arm			
<i>(millions of Canadian dollars)</i>													
For the year ended December 31, 2016													
Energy sales	511	40	-	-	96	-	43	-	131	-	-	(42)	779
Other revenue	4	-	-	-	1	6	-	-	9	21	-	4	45
Revenue	515	40	-	-	97	6	43	-	140	21	-	(38)	824
Fuels	168	-	-	-	-	-	-	-	-	-	-	-	168
Power purchased	60	39	-	-	-	-	4	-	-	-	-	(42)	61
Operating costs	124	4	-	2	44	3	5	-	8	1	13	3	207
Production, marketing and transportation costs	-	-	-	-	-	-	-	-	26	-	-	-	26
Transmission rental and market fees	-	-	-	-	-	-	22	-	-	-	-	-	22
Depreciation, depletion, amortization and impairment	68	-	-	-	17	-	-	1	48	-	1	-	135
Exploration and evaluation	-	-	-	-	-	-	-	-	2	-	-	-	2
Net finance expense (income)	71	-	-	(2)	(1)	-	-	-	3	-	1	-	72
Other expense (income)	6	-	1	(1)	-	-	(5)	-	(5)	-	-	-	(4)
Preferred dividends	-	-	-	-	(4)	-	-	-	-	-	-	4	-
Expenses	497	43	1	(1)	56	3	26	1	82	1	15	(35)	689
Profit (loss) before regulatory adjustments	18	(3)	(1)	1	41	3	17	(1)	58	20	(15)	(3)	135
Regulatory adjustments	(1)	-	-	-	-	-	-	-	-	-	-	-	(1)
Profit (loss) for the year	19	(3)	(1)	1	41	3	17	(1)	58	20	(15)	(3)	136
Capital expenditures*	221	1	976	1,315	41	491	-	1	236	-	6	(2)	3,286
Total assets**	2,442	51	3,598	4,731	560	1,183	8	187	1,243	4	384	(328)	14,063
Total debt***	1,182	-	2,055	3,346	-	-	-	-	-	-	-	-	6,583

*Capital expenditures (inclusive of property, plant and equipment and intangible assets) include non-cash additions of \$485.2 million related to the Maritime Link and \$23.6 million related to Class B Limited Partnership Unit accrued interest.

**Total assets include \$1,146.5 million related to the Maritime Link and \$37.4 million related to Class B Limited Partnership Unit accrued interest.

***Total debt includes short-term borrowings, long-term debt including current portion less Hydro's sinking funds of \$267.0 million, and Class B Limited Partnership Units.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

35. SUBSEQUENT EVENT

On March 8, 2018, the Province of Newfoundland and Labrador issued long-term debt with a face value of \$300.0 million, specifically on Hydro's behalf. The debt matures on October 17, 2048 with a coupon rate of 3.70% paid semi-annually. Nalcor expects to use a portion of the proceeds to repay the \$225.0 million promissory note to the Province.

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