

MUSKRAT FALLS CORPORATION
FINANCIAL STATEMENTS
December 31, 2022

Independent Auditor's Report

To the Shareholder of Muskrat Falls Corporation

Opinion

We have audited the financial statements of Muskrat Falls Corporation (the "Company"), which comprise the statement of financial position as at December 31, 2022, and the statement of profit (loss) and comprehensive income (loss), changes in equity and cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies (collectively referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2022, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

Basis for Opinion

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

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

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

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

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

Auditor's Responsibilities for the Audit of the Financial Statements

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

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

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

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

Deloitte LLP

Chartered Professional Accountants
March 21, 2023

MUSKRAT FALLS CORPORATION
STATEMENT OF FINANCIAL POSITION

| <i>As at December 31 (thousands of Canadian dollars)</i> | Notes | 2022 | 2021 |
|--|-------|------------------|-----------|
| ASSETS | | | |
| Current assets | | | |
| Restricted cash | | 783,017 | 420,674 |
| Trade and other receivables | 5 | 28,722 | 3,993 |
| Related party loan receivable | 17 | 3,374 | 9,843 |
| Short-term investments | 7 | 34,372 | - |
| Contract asset | 8 | 165,466 | 17,573 |
| Other current assets | | 2,035 | 2,600 |
| Total current assets | | 1,016,986 | 454,683 |
| Non-current assets | | | |
| Property, plant and equipment | 6 | 6,427,204 | 6,398,742 |
| Investments | 7 | 200,557 | - |
| Other long-term asset | 17 | 3,126 | 3,014 |
| Total assets | | 7,647,873 | 6,856,439 |
| LIABILITIES AND EQUITY | | | |
| Current liabilities | | | |
| Trade and other payables | 9 | 66,566 | 169,609 |
| Current portion of long-term debt | 10 | 34,372 | 33,872 |
| Current portion of long-term payables | 11 | 46,639 | 44,309 |
| Related party loan payable | 17 | 29,665 | 53,220 |
| Total current liabilities | | 177,242 | 301,010 |
| Non-current liabilities | | | |
| Long-term debt | 10 | 4,430,022 | 3,630,194 |
| Long-term payables | 11 | 160,686 | 88,795 |
| Total liabilities | | 4,767,950 | 4,019,999 |
| Shareholder's equity | | | |
| Share capital | 12 | 1,801,807 | 1 |
| Shareholder contributions | | 1,169,486 | 3,011,317 |
| Reserves | | (45,120) | (48,143) |
| Deficit | | (46,250) | (126,735) |
| Total equity | | 2,879,923 | 2,836,440 |
| Total liabilities and equity | | 7,647,873 | 6,856,439 |

Commitments and contingencies (Note 18)

See accompanying notes

On behalf of the Board:



DIRECTOR



DIRECTOR

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

| <i>For the year ended December 31 (thousands of Canadian dollars)</i> | Notes | 2022 | 2021 |
|---|-------|----------------|-----------|
| Revenue | 17 | 491,263 | 67,146 |
| Total revenue | | 491,263 | 67,146 |
| Power purchased | 17 | 5,893 | 3,957 |
| Operating costs | 13 | 29,384 | 13,250 |
| Transmission expense | 17 | 118,305 | 136,079 |
| Depreciation | | 237 | 14 |
| Net finance expense | 14 | 119,456 | 13,563 |
| Other expense | 15 | 19,057 | 3,576 |
| Total expenses | | 292,332 | 170,439 |
| Profit (loss) for the year | | 198,931 | (103,293) |
| Other comprehensive income | | | |
| Total items that may or have been reclassified to profit or loss: | | | |
| Reclassification adjustment related to: | | | |
| Cash flow hedges recognized in profit or loss | | 3,023 | 3,046 |
| Other comprehensive income for the year | | 3,023 | 3,046 |
| Total comprehensive income (loss) for the year | | 201,954 | (100,247) |

See accompanying notes

MUSKRAT FALLS CORPORATION
STATEMENT OF CHANGES IN EQUITY

| <i>(thousands of Canadian dollars)</i> | Notes | Share Capital | Shareholder Contributions | Reserves | Deficit | Total |
|--|-------|------------------|------------------------------|-----------------|------------------|------------------|
| Balance at January 1, 2022 | | 1 | 3,011,317 | (48,143) | (126,735) | 2,836,440 |
| Profit for the year | | - | - | - | 198,931 | 198,931 |
| Other comprehensive income | | - | - | 3,023 | - | 3,023 |
| Total comprehensive income for the year | | - | - | 3,023 | 198,931 | 201,954 |
| Shareholder contributions | 17 | - | 5,893 | - | - | 5,893 |
| Capital restructuring | 12 | 1,847,724 | (1,847,724) | - | - | - |
| Share redemption | 12 | (45,918) | - | - | - | (45,918) |
| Dividends | 12 | - | - | - | (43,678) | (43,678) |
| Related party transaction | 17 | - | - | - | (74,768) | (74,768) |
| Balance at December 31, 2022 | | 1,801,807 | 1,169,486 | (45,120) | (46,250) | 2,879,923 |
| Balance at January 1, 2021 | | 1 | 2,783,975 | (51,189) | (14,852) | 2,717,935 |
| Loss for the year | | - | - | - | (103,293) | (103,293) |
| Other comprehensive income | | - | - | 3,046 | - | 3,046 |
| Total comprehensive loss for the year | | - | - | 3,046 | (103,293) | (100,247) |
| Shareholder contributions | | - | 267,622 | - | - | 267,622 |
| Distribution of contributed capital | | - | (40,280) | - | - | (40,280) |
| Related party transaction | 17 | - | - | - | (8,590) | (8,590) |
| Balance at December 31, 2021 | | 1 | 3,011,317 | (48,143) | (126,735) | 2,836,440 |

See accompanying notes

MUSKRAT FALLS CORPORATION
STATEMENT OF CASH FLOWS

| <i>For the year ended December 31 (thousands of Canadian dollars)</i> | Notes | 2022 | 2021 |
|--|-------|------------------|-----------|
| Operating activities | | | |
| Profit (loss) for the year | | 198,931 | (103,293) |
| Adjustments to reconcile profit (loss) to cash provided from (used in) operating activities: | | | |
| Depreciation and amortization | | 3,260 | 334 |
| Revenue | 17 | (74,768) | (8,590) |
| Power purchased | 17 | 5,893 | 3,957 |
| Finance income | 14 | (24,791) | (2,265) |
| Finance expense | 14 | 144,247 | 15,828 |
| | | 252,772 | (94,029) |
| Changes in non-cash working capital balances | 20 | (7,804) | 17,889 |
| Increase in long-term payables | | 74,221 | 129,357 |
| Increase in contract asset | | (147,893) | (17,573) |
| Increase in other long-term asset | | (112) | (3,014) |
| Interest received | | 21,092 | 1,984 |
| Interest paid | | (142,888) | (129,048) |
| Net cash provided from (used in) operating activities | | 49,388 | (94,434) |
| Investing activities | | | |
| Change in related party loan receivable | | 6,433 | (9,792) |
| Increase in investments | 7 | (234,929) | - |
| Change in advances | | 839 | (173) |
| Additions to property, plant and equipment | | (32,287) | (191,296) |
| Changes in non-cash working capital balances | 20 | (114,522) | (13,641) |
| Net cash used in investing activities | | (374,466) | (214,902) |
| Financing activities | | | |
| Change in restricted cash | | (362,343) | 66,449 |
| Change in related party loan payable | | (23,399) | 52,931 |
| Proceeds from long-term debt | | 834,288 | - |
| Repayment of long-term debt | | (33,872) | (33,429) |
| Share redemption | 12 | (45,918) | - |
| Dividends | 12 | (43,678) | - |
| Shareholder contributions | | - | 263,665 |
| Distribution of contributed capital | | - | (40,280) |
| Net cash provided from financing activities | | 325,078 | 309,336 |
| Net increase (decrease) in cash | | - | - |
| Cash, beginning of the year | | - | - |
| Cash, end of the year | | - | - |

See accompanying notes

MUSKRAT FALLS CORPORATION

NOTES TO THE FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS

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

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

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

2. SIGNIFICANT ACCOUNTING POLICIES

2.1 Statement of Compliance and Basis of Measurement

These annual audited financial statements (financial statements) have been prepared in accordance with International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB).

These financial statements have been prepared on a historical cost basis and are presented in Canadian Dollars (CAD) with all values rounded to the nearest thousand, except when otherwise noted. The financial statements were approved by Muskrat Falls' Board of Directors on March 9, 2023.

2.2 Basis of Consolidation

The financial statements include only the financial statements of Muskrat Falls.

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

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

The Muskrat Falls/Labrador Transmission Assets Funding Trust (MF/LTA Funding Trust) was formed under the laws of the Province and the federal laws of Canada on November 4, 2013 for the purpose of issuing long-term debentures to the public, which are guaranteed by the Government of Canada (Canada), and to on-lend the proceeds to Muskrat Falls and Labrador Transco. The funds provide financing for the MF Plant and the Labrador Transmission Assets as part of Phase 1 of the Lower Churchill Project.

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

MUSKRAT FALLS CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

2.3 Restricted Cash

Restricted cash consists of cash held on deposit with a Schedule 1 Canadian Chartered Bank and administered by the Collateral Agent for the sole purpose of funding construction, operating, maintenance, sustaining and financing costs related to the MF Plant, including pre-funded equity amounts required under the MF/LTA Project Finance Agreement (MF/LTA PFA). The Company draws funds from this account on a monthly basis in accordance with procedures set out in the MF/LTA PFA. Restricted cash also includes funds held in trust by solicitors of the Company.

2.4 Short-term Investments

Investments with maturities greater than three months and less than twelve months are considered short-term investments.

2.5 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 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.

2.6 Property, Plant and Equipment

Items of property, plant and equipment are recognized at cost less accumulated depreciation and accumulated impairment losses. Cost includes materials, labour, contracted services, professional fees and, for qualifying assets, borrowing costs capitalized in accordance with Muskrat Falls' accounting policy outlined in Note 2.7. 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, Muskrat Falls recognizes such parts as individual assets with specific useful lives and depreciation rates. Likewise, when a major inspection is performed, its cost is recognized in the carrying amount of the asset as a replacement if the recognition criteria are satisfied. All other repairs and maintenance costs are recognized in profit or loss as incurred.

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

| | |
|--------------------------------|-----------------|
| Project support assets | 6 to 7 years |
| Hydroelectric generation plant | 15 to 100 years |
| Service facilities and other | 5 to 100 years |

Hydroelectric generation plant includes the powerhouse, turbines and generators, governors and exciters, and auxiliary systems, as well as water conveying and control structures, including dams, tailraces, spillway, penstocks, draft tube and intake structures.

Service facilities and other include roads, telecontrol, buildings, vehicles, heavy equipment, furniture, and tools and equipment.

The carrying amount of a replaced asset is derecognized when replaced. Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment and are recorded in other expense.

2.7 Borrowing Costs

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

2.8 Impairment of Non-Financial Assets

Property, plant and equipment and other non-financial assets are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Where it is not possible to estimate the recoverable amount of an individual asset, Muskrat Falls estimates the recoverable amount of the cash generating unit (CGU) to which the asset belongs. The recoverable amount is the higher of fair value less costs of disposal and value in use. Value in use is generally computed by reference to the present value of future cash flows expected to be derived from non-financial assets. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset or CGU is estimated to be less than its carrying amount, the carrying amount of the asset or CGU is reduced to its recoverable amount and an impairment loss is recognized immediately in the Statement of Profit (Loss) and Comprehensive Income (Loss).

2.9 Provisions

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

2.10 Revenue Recognition

Muskrat Falls recognizes revenue from contracts with customers related to the sale of electricity. Revenue is measured based on the consideration specified in the contract with a customer, forecasted over the term of the contract and constrained where applicable. Sales are at rates under the terms of the applicable contracts, or at market rates.

Revenue is recognized when Muskrat Falls satisfies its performance obligations and is determined when it transfers control of a product or service to a customer. Variable components that meet the allocation exemption are recognized as incurred. A contract asset/liability is recognized when the timing of satisfying the performance obligations and the timing of contractual payments are not aligned.

2.11 Leasing

Lessee Accounting

Muskrat Falls assesses whether a contract is or contains a lease, at inception of a contract. Muskrat Falls recognizes a right-of-use asset and a corresponding lease liability with respect to all lease agreements in which it is the lessee, except for short-term leases (defined as leases with a lease term of 12 months or less) and leases of low-value assets. For these leases, Muskrat Falls recognizes the lease payments as an operating expense on a straight-line basis over the term of the lease unless another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

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

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

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

MUSKRAT FALLS CORPORATION
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The lease liability is subsequently measured at amortized cost using the effective interest rate method. Lease liabilities are remeasured, with a corresponding adjustment to the related right-of-use assets, when there is a change in variable lease payments arising from a change in an index or rate, or when Muskrat Falls changes its assessment of whether purchase, renewal or termination options will be exercised. Muskrat Falls did not make any such adjustments during the periods presented.

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

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

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

Variable rents that do not depend on an index or rate are not included in the measurement of the lease liability and the right-of-use asset. The related payments are recognized as an expense in operating costs in the period in which the event or condition that triggers those payments occurs.

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

2.12 Foreign Currencies

Transactions in currencies other than Muskrat Falls' functional currency (foreign currencies) are recognized using the exchange rate in effect at the date of transaction, approximated by the prior month end close rate. At the end of each reporting period, monetary items denominated in foreign currencies are translated at the rates of exchange in effect at the period end date. Foreign exchange gains and losses are included in the Statement of Profit (Loss) and Comprehensive Income (Loss) as other expense.

2.13 Income Taxes

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

2.14 Financial Instruments

Classification and Initial Measurement

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

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

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NOTES TO THE FINANCIAL STATEMENTS

Financial Assets at Amortized Cost

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

Musktrat Falls' financial assets at amortized cost include restricted cash, trade and other receivables, related party loan receivable and investments (including short-term).

Financial Liabilities at Amortized Cost

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

Musktrat Falls' financial liabilities at amortized cost include trade and other payables, related party loan payable, long-term debt and long-term payables.

Derecognition of Financial Instruments

Musktrat Falls derecognizes a financial asset when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another party.

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

Impairment of Financial Assets

Musktrat Falls recognizes a loss allowance for expected credit losses (ECL) on investments in debt instruments that are measured at amortized cost. The amount of ECL is updated at each reporting date to reflect changes in credit risk since initial recognition of the respective financial instrument.

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

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

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

Hedges

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

The effective portion of the gain or loss on a cash flow hedging instrument is recognized directly in other comprehensive income, while any ineffective portion is recognized immediately in the Statement of Profit (Loss) and Comprehensive Income (Loss) for the period in other expense. Amounts recognized in other comprehensive income are transferred to the Statement of Profit (Loss) and Comprehensive Income (Loss) 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.

Musktrat Falls does not hold any fair value hedges.

3. SIGNIFICANT ACCOUNTING JUDGMENTS AND ESTIMATES

The preparation of the financial statements in conformity with IFRS requires Management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, revenues and expenses. Actual results may differ materially from these estimates. The estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognized in the period in which the estimate is reviewed if the revision affects only that period or future periods.

3.1 Use of Judgments

(i) Asset Impairment and Reversals

Musktrat Falls 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 judgment in selecting discount rates and considering the occurrence of future events when determining the recoverable amount. 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

Musktrat Falls' accounting policy relating to property, plant and equipment is described in Note 2.6. 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 Musktrat Falls' property, plant and equipment.

(iii) Revenue

Management uses judgment in estimating the variable consideration in a contract, such as future sustaining capital costs, and assessing whether a variable component is constrained. Management also uses judgment in allocating amounts to performance obligations and determining the timing of satisfaction of performance obligations. Revenue related to electricity sales is allocated between energy and capacity components based on observable evidence of how efficiently island rate payers use the hydroelectric system. Energy is recognized as units are delivered whereas capacity is recognized evenly over the time elapse of the term.

MUSKRAT FALLS CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

(iv) Functional Currency

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

(v) Determination of CGUs

Musktrat Falls' accounting policy relating to impairment of non-financial assets is described in Note 2.8. In applying this policy, Musktrat Falls 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) Consolidation

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

(vii) Leases

Definition of a Lease

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

Lease Extension and Termination Options

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

3.2 Use of Estimates

(i) Property, Plant and Equipment

Amounts recorded for depreciation are based on the useful lives of the Company's assets. The useful lives of property, plant and equipment are verified by independent specialists and reviewed annually by the Company. The 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) Leases Incremental Borrowing Rate

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

4. CURRENT AND FUTURE CHANGES IN ACCOUNTING POLICIES

The following is a list of amendments that have been issued and are effective for accounting periods commencing on or after January 1, 2022, as specified.

- *IAS 37 – Provisions, Contingent Liabilities and Contingent Assets – Onerous Contracts – Costs of Fulfilling a Contract (Amendments to IAS 37)*¹
- *IAS 1 – Presentation of Financial Statements– Disclosure of Accounting Policies (Amendments to IAS 1)*²
- *IAS 8 – Accounting Policies, Changes in Accounting Estimates and Errors – Definition of Accounting Estimates (Amendments to IAS 8)*²
- *IAS 1 – Presentation of Financial Statements – Classification of Liabilities as Current or Non-Current (Amendments to IAS 1)*³

¹ Effective for annual periods beginning on or after January 1, 2022.

² Effective for annual periods beginning on or after January 1, 2023, with earlier application permitted.

³ These amendments were originally effective for annual periods beginning on or after January 1, 2023, however, in 2022 the IASB deferred the effective date to January 1, 2024, with earlier application permitted.

4.1 IAS 37 – Provisions, Contingent Liabilities and Contingent Assets – Onerous Contracts – Costs of Fulfilling a Contract (Amendments to IAS 37)

The amendments to IAS 37 specify that the cost of fulfilling a contract comprises the costs that relate directly to the contract. Costs that relate directly to a contract can either be incremental costs of fulfilling that contract, such as direct labour and materials, or an allocation of other costs that relate directly to fulfilling contracts, such as the allocation of the depreciation charge for an item of property, plant and equipment used in fulfilling the contract. These amendments apply to contracts for which the entity has not yet fulfilled all its obligations at the beginning of the annual reporting period in which the entity first applies the amendments and are currently not applicable to Muskrat Falls however, may apply to future transactions.

4.2 IAS 1 – Presentation of Financial Statements– Disclosure of Accounting Policies (Amendments to IAS 1)

The IASB issued amendments to IAS 1, which change the requirements with regard to the disclosure of accounting policies. The amendments replace all instances of the term ‘significant accounting policies’ with ‘material accounting policy information’. Accounting policy information is material if, when considered together with other information included in an entity’s financial statements, it can reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements. Management does not expect this change will have a material impact on the financial statements.

4.3 IAS 8 – Accounting Policies, Changes in Accounting Estimates and Errors – Definition of Accounting Estimates (Amendments to IAS 8)

The IASB issued amendments to IAS 8 to clarify the distinction between changes in accounting estimates and changes in accounting policies and the correction of errors. The amendments are intended to improve the understanding of the existing requirements and therefore will not have an impact on Muskrat Falls’ financial statements.

4.4 IAS 1 – Presentation of Financial Statements – Classification of Liabilities as Current or Non-Current (Amendments to IAS 1)

The IASB issued amendments to IAS 1 to promote consistency in applying the requirements by helping companies determine whether, in the Statement of Financial Position, debt and other liabilities with an uncertain settlement date should be classified as current (due or potentially due to be settled within one year) or non-current. The classification is based on rights that are in existence at the end of the reporting period and specify that classification is unaffected by expectations about whether an entity will exercise its right to defer settlement of a liability. Additional information was added to clarify that only covenants with which an entity is required to comply on or before the reporting date affect the classification of a liability as current or non-current. In addition, an entity has to disclose information in the notes that enables users of financial statements to understand the risk that non-current liabilities with covenants could become repayable within twelve months. The amendments are applied retrospectively upon adoption. The application of these amendments is not expected to have a material impact on Muskrat Falls’ financial statements.

MUSKRAT FALLS CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

5. TRADE AND OTHER RECEIVABLES

| <i>As at December 31 (thousands of Canadian dollars)</i> | 2022 | 2021 |
|--|---------------|-------|
| Due from related parties | 23,431 | 2,699 |
| Interest receivable | 3,803 | 156 |
| HST receivable | 1,309 | 1,138 |
| Trade receivables | 179 | - |
| | 28,722 | 3,993 |

6. PROPERTY, PLANT AND EQUIPMENT

| <i>(thousands of Canadian dollars)</i> | Project Support Assets | Construction in Progress | Other | Total |
|--|---------------------------|-----------------------------|--------------|------------------|
| Cost | | | | |
| Balance at January 1, 2021 | 193,666 | 6,090,275 | 918 | 6,284,859 |
| Additions | - | 307,014 | 705 | 307,719 |
| Balance at December 31, 2021 | 193,666 | 6,397,289 | 1,623 | 6,592,578 |
| Additions | - | 30,305 | 1,982 | 32,287 |
| Other adjustments | - | (3,588) | - | (3,588) |
| Balance at December 31, 2022 | 193,666 | 6,424,006 | 3,605 | 6,621,277 |
| Depreciation | | | | |
| Balance at January 1, 2021 | 193,666 | - | 29 | 193,695 |
| Depreciation | - | - | 141 | 141 |
| Balance at December 31, 2021 | 193,666 | - | 170 | 193,836 |
| Depreciation | - | - | 237 | 237 |
| Balance at December 31, 2022 | 193,666 | - | 407 | 194,073 |
| Carrying value | | | | |
| Balance at January 1, 2021 | - | 6,090,275 | 889 | 6,091,164 |
| Balance at December 31, 2021 | - | 6,397,289 | 1,453 | 6,398,742 |
| Balance at December 31, 2022 | - | 6,424,006 | 3,198 | 6,427,204 |

Capitalized Borrowing Costs

The construction of the MF Plant is being financed through the issuance of long-term debt and contributed capital. For the year ended December 31, 2022, \$(3.6) million (2021 - \$113.4 million) of borrowing costs were capitalized.

MUSKRAT FALLS CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

7. INVESTMENTS

The following table represents the value of the investments measured at amortized cost:

| <i>As at December 31 (thousands of Canadian dollars)</i> | Year of Maturity | 2022 | 2021 |
|---|---------------------|-----------------|------|
| Amortizing Fixed Rate Deposit Notes with interest paid at a rate of 3.745% per annum. | 2023- 2029 | 234,929 | - |
| Less: redemptions to be received within one year | | (34,372) | - |
| | | 200,557 | - |

On March 31, 2022, the Company, jointly with Labrador Transco, purchased structured deposit notes using the proceeds from issued long-term debt. The investments are restricted in nature and subject to the provisions contained within the MF/LTA PFA. Muskrat Falls recognizes 83.43% of these investments which is based on its cumulative portion of actual debt drawn for the construction of the MF Plant.

8. CONTRACT ASSET

| <i>As at December 31 (thousands of Canadian dollars)</i> | 2022 | 2021 |
|--|------------------|----------|
| Contract asset, beginning of the year | 17,573 | - |
| Additions | 389,444 | 57,450 |
| Less: Receipts | (241,551) | (39,877) |
| Contract asset, end of the year | 165,466 | 17,573 |

The contract asset represents the timing difference between the satisfaction of performance obligations to Hydro under the PPA and the timing of commercial payments.

9. TRADE AND OTHER PAYABLES

| <i>As at December 31 (thousands of Canadian dollars)</i> | 2022 | 2021 |
|--|---------------|---------|
| Due to related parties | 28,212 | 14,027 |
| Trade payables and accruals | 25,821 | 141,063 |
| Accrued interest | 12,394 | 14,467 |
| HST payable | 139 | 52 |
| | 66,566 | 169,609 |

MUSKRAT FALLS CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

10. LONG-TERM DEBT

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

| <i>As at (thousands of Canadian dollars)</i> | Face Value | Coupon Rate % | Year of Issue | Year of Maturity | 2022 | 2021 |
|---|------------------|---------------|---------------|------------------|------------------|-----------|
| Tranche A | 542,287 | 3.63 | 2013 | 2029 | 542,368 | 542,381 |
| Tranche B | 563,144 | 3.83 | 2013 | 2037 | 563,200 | 563,204 |
| Tranche C | 1,063,717 | 3.86 | 2013 | 2048 | 1,063,875 | 1,063,881 |
| Tranche 6-10 | 86,919 | 1.52-1.75 | 2017 | 2023-2025 | 86,924 | 120,799 |
| Tranche 11-20 | 187,117 | 1.84-2.37 | 2017 | 2025-2030 | 187,144 | 187,149 |
| Tranche 21-30 | 210,737 | 2.41-2.64 | 2017 | 2030-2035 | 210,811 | 210,819 |
| Tranche 31-40 | 240,429 | 2.66-2.80 | 2017 | 2035-2040 | 240,625 | 240,638 |
| Tranche 41-50 | 276,180 | 2.81-2.86 | 2017 | 2040-2045 | 276,422 | 276,434 |
| Tranche 51-60 | 317,934 | 2.84-2.86 | 2017 | 2045-2050 | 318,303 | 318,318 |
| Tranche 61-64 | 140,205 | 2.85 | 2017 | 2050-2052 | 140,434 | 140,443 |
| Tranche A-T | 417,144 | 3.35-3.38 | 2022 | 2037-2047 | 417,144 | - |
| Tranche U | 417,144 | 3.38 | 2022 | 2057 | 417,144 | - |
| Total | 4,462,957 | | | | 4,464,394 | 3,664,066 |
| Less: maturities of debt within one year | | | | | (34,372) | (33,872) |
| | | | | | 4,430,022 | 3,630,194 |

Muskrat Falls, MF/LTA Funding Trust, Labrador Transco and the Collateral Agent have entered into the MF/LTA PFA. Under the terms and conditions of the MF/LTA PFA, the MF/LTA Funding Trust agreed to provide three credit facilities. The first credit facility was issued in November 2013 (Tranche A, B and C) for \$2.6 billion, the second credit facility was issued in May 2017 (Tranche 1-64) for \$1.85 billion and the third credit facility was issued in March 2022 for \$1.0 billion for a combined total of \$5.45 billion. Muskrat Falls and Labrador Transco are jointly and severally liable for the full amount of the credit facilities. Muskrat Falls' recognizes 83.43% of the debt, which is based on its cumulative portion of actual debt drawn for the construction of the MF Plant. The financing of the MF/LTA Funding Trust benefits from a direct, absolute, unconditional and irrevocable guarantee from Canada, and thereby carries its full faith and credit (AAA rating or equivalent).

The role of the Collateral Agent is to act on behalf of the lending parties, including the MF/LTA Funding Trust and Canada. The Collateral Agent oversees the lending and security arrangements, the various project accounts and the compliance with covenants. As security for these debt obligations, Muskrat Falls has granted to the Collateral Agent first ranking liens on all present and future assets. Sinking funds are required to be set up for the Tranche B and C debentures and are to be held in a sinking fund account under the control of the Collateral Agent with payments beginning in 2029. The sinking fund payment originally required for Tranche A was removed as part of an amendment to the MF/LTA PFA in March 2022.

MUSKRAT FALLS CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

11. LONG-TERM PAYABLES

| <i>As at December 31 (thousands of Canadian dollars)</i> | 2022 | 2021 |
|--|-----------------|-------------|
| Long-term payables, beginning of the year | 133,104 | 3,747 |
| Additions | 111,937 | 134,948 |
| Less: Settlements | (37,716) | (5,591) |
| Long-term payables, end of the year | 207,325 | 133,104 |
| Less: current portion | (46,639) | (44,309) |
| | 160,686 | 88,795 |

The long-term payable represents the difference between receipt of services from Labrador Transco under the GIA and the timing of commercial payments.

12. SHAREHOLDER'S EQUITY

12.1 Share Capital

| <i>As at December 31 (thousands of Canadian dollars)</i> | 2022 | 2021 |
|--|------------------|-------------|
| Class A preferred shares without nominal or par value | | |
| Authorized – unlimited | | |
| Issued - fully paid and outstanding - 1,801,806,139 (2021 – nil) | 1,801,806 | - |
| Class A common shares without nominal or par value | | |
| Authorized – unlimited | | |
| Issued - fully paid and outstanding - 1,000 (2021 – nil) | 1 | - |
| Common shares without nominal or par value | | |
| Authorized – unlimited | | |
| Issued - fully paid and outstanding – 0 (2021 – 100) | - | 1 |
| | 1,801,807 | 1 |

On March 25, 2022, the Company amended its Articles of Incorporation to create a new capital structure. Included in the new capital structure, previously held common shares were designated Class A common shares and Class A preferred shares increased by \$1,847.7 million. On May 13, 2022, the Company redeemed 45.9 million Class A preferred shares of \$45.9 million (2021 - \$nil).

12.2 Dividends

| <i>For the year ended December 31 (thousands of Canadian dollars)</i> | 2022 | 2021 |
|---|---------------|-------------|
| Declared and paid during the year | | |
| Preferred dividend for current year (3% coupon rate) | 41,799 | - |
| Common dividend for current year | 1,879 | - |
| | 43,678 | - |

13. OPERATING COSTS

| <i>For the year ended December 31 (thousands of Canadian dollars)</i> | 2022 | 2021 |
|---|---------------|-------------|
| Professional services | 9,262 | 3,189 |
| Salaries and benefits | 7,041 | 4,173 |
| Maintenance and materials | 6,828 | 4,127 |
| Other operating costs | 3,145 | 1,484 |
| Insurance | 3,108 | 277 |
| | 29,384 | 13,250 |

MUSKRAT FALLS CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

14. NET FINANCE EXPENSE

| <i>For the year ended December 31 (thousands of Canadian dollars)</i> | 2022 | 2021 |
|---|----------------|-----------|
| Finance income | | |
| Interest on restricted cash | 17,419 | 2,122 |
| Interest on investments | 7,166 | - |
| Other interest | 206 | 143 |
| | 24,791 | 2,265 |
| Finance expense | | |
| Interest and fees on long-term debt | 137,728 | 128,890 |
| Other interest | 2,931 | 298 |
| | 140,659 | 129,188 |
| Interest capitalized during construction | 3,588 | (113,360) |
| | 144,247 | 15,828 |
| Net finance expense | 119,456 | 13,563 |

15. OTHER EXPENSE

| <i>For the year ended December 31 (thousands of Canadian dollars)</i> | 2022 | 2021 |
|---|---------------|-------|
| Rental and royalty | 12,860 | 2,660 |
| Other | 6,197 | 916 |
| Other expense | 19,057 | 3,576 |

16. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

16.1 Fair Value

The estimated fair values of financial instruments as at December 31, 2022 and 2021 are based on relevant market prices and information available at the time. Fair value estimates are based on valuation techniques which are significantly affected by the assumptions used including the amount and timing of future cash flows and discount rates reflecting various degrees of risk. As such, the fair value estimates disclosed are not necessarily indicative of the amounts that Muskrat Falls might receive or incur in actual market transactions.

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

Establishing Fair Value

Financial instruments recorded at fair value are classified using a fair value hierarchy that reflects the nature of the inputs used in making the measurements. The fair value hierarchy has the following levels:

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

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

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

MUSKRAT FALLS CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value. For assets and liabilities that are recognized at fair value on a recurring basis, the Company determines whether transfers have occurred between levels in the hierarchy by reassessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period. There were no transfers between Level 1, 2 and 3 fair value measurements during the years ended December 31, 2022 and 2021.

As at December 31, 2022 and 2021, the Company did not have any Level 3 instruments.

| | Level | Carrying Value | Fair Value | Carrying Value | Fair Value |
|---|-------|-------------------|------------|-------------------|------------|
| | | December 31, 2022 | | December 31, 2021 | |
| <i>(thousands of Canadian dollars)</i> | | | | | |
| Financial assets | | | | | |
| Investments, including short-term | 2 | 234,929 | 220,225 | - | - |
| Financial liabilities | | | | | |
| Long-term debt including amount due within one year | 2 | 4,464,394 | 4,011,750 | 3,664,066 | 4,252,086 |

The fair values of restricted cash, trade and other receivables, related party loan receivable, trade and other payables and related party loan payable approximate their carrying values due to their short-term maturity. The fair value of the long-term payables approximates its carrying value due to the underlying nature of the balance with its intercompany counterparty.

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

16.2 Risk Management

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

Credit Risk

The Company's expected future cash flows are exposed to credit risk through financing activities, based on the risk of non-performance by counterparties to its financial instruments. Credit risk on restricted cash and investments is minimal, as the Company's deposits are held by a Canadian Schedule 1 Chartered Bank with a rating of A+ and AA- (Standard and Poor's). The degree of exposure to credit risk on trade and other receivables is determined by the financial capacity and stability of the counterparties whereby the maximum risk is represented by their carrying value on the Statement of Financial Position at the reporting date.

Liquidity Risk

The Company is exposed to liquidity risk with respect to its contractual obligations and financial liabilities, including derivative liabilities relating to hedging activities. Liquidity risk management activities are directed at ensuring cash is available to meet those obligations as they become due. Short-term liquidity is provided through restricted cash on hand, related party loans and shareholder contributions.

MUSKRAT FALLS CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

The following are the contractual maturities of the Company's financial liabilities, including principal, interest and sinking fund as at December 31, 2022:

| <i>(thousands of Canadian dollars)</i> | < 1 Year | 1-3 Years | 3-5 Years | > 5 Years | Total |
|--|----------|-----------|-----------|-----------|-----------|
| Trade and other payables | 66,566 | - | - | - | 66,566 |
| Related party loan payable | 29,665 | - | - | - | 29,665 |
| Long-term payables | 46,639 | 93,862 | 66,824 | - | 207,325 |
| Long-term debt | 182,931 | 365,903 | 365,971 | 6,491,653 | 7,406,458 |
| | 325,801 | 459,765 | 432,795 | 6,491,653 | 7,710,014 |

Market Risk

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

Interest Rates

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

In May 2017, Muskrat Falls entered into three bond forward contracts, jointly with Labrador Transco, to hedge the interest rate risk on the forecasted issue of the additional long-term debt. Muskrat Falls' prorated share of these contracts was \$1.4 billion. These contracts were designated as part of a cash flow hedging relationship and the resulting change in fair value of \$52.0 million was recorded in other comprehensive income (loss) with the ineffective portion of \$0.9 million recognized immediately in other (income) expense. The amortization of the other comprehensive loss related to the effective portion of the cash flow hedge was capitalized in prior years and is amortized to profit or loss for the current year in line with treatment of the interest expense related to the long-term debt that it is hedging, in accordance with Muskrat Falls' accounting policy outlined in Note 2.7. The total amount amortized in 2022 including the previous cash flow hedge initiated in December 2013 was \$3.0 million (2021 - \$3.0 million).

Foreign Currency and Commodity Exposure

The Company does not hold any financial instruments whose value would vary due to changes in a commodity price or whose value would materially vary due to fluctuations in foreign currency exchange rates. Cash flow exposure to foreign exchange risk arises primarily through investing activities, most notably US dollar denominated capital expenditures, and regular procurement activities.

17. RELATED PARTY TRANSACTIONS

Muskrat Falls enters into various transactions with its parent and other related parties. Unless otherwise noted, 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. Outstanding balances due to or from related parties are non-interest bearing with settlement within 30 days, unless otherwise stated.

MUSKRAT FALLS CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

Related parties with which Muskrat Falls transacts are as follows:

| Related Party | Relationship |
|--|---|
| Nalcor | 100% shareholder of Muskrat Falls |
| Hydro | Wholly-owned subsidiary of Nalcor |
| Labrador Transco | Wholly-owned subsidiary of Nalcor |
| Lower Churchill Management Corporation | Wholly-owned subsidiary of Nalcor |
| Labrador-Island Link Limited Partnership | Limited partnership between Labrador-Island Link Holding Corporation and Emera Newfoundland and Labrador Island Link Inc. |
| Nalcor Energy Marketing Corporation | Wholly-owned subsidiary of Nalcor |
| Churchill Falls (Labrador) Corporation | Joint arrangement of Hydro |
| The Province | 100% shareholder of Nalcor |

Significant related party transactions, which are not otherwise disclosed separately in the financial statements, are summarized below:

| <i>As at December 31 (thousands of Canadian dollars)</i> | 2022 | 2021 |
|---|---------|---------|
| Trade and other receivables: | | |
| Other related parties | 23,431 | 2,699 |
| Related party loan receivable: | | |
| Other related parties (a) | 3,374 | 9,843 |
| Contract asset: | | |
| Other related parties Note 8 | 165,466 | 17,573 |
| Other long-term asset: | | |
| Other related parties Note 18(d) | 3,126 | 3,014 |
| Trade and other payables: | | |
| Parent | 7,769 | 7,487 |
| The Province | 12,968 | 5,663 |
| Other related parties | 7,475 | 877 |
| Related party loan payable: | | |
| Other related parties (b) | 29,665 | 53,220 |
| Long-term payables (including current portion): | | |
| Other related parties Note 11 | 207,325 | 133,104 |
| <i>For the year ended December 31 (thousands of Canadian dollars)</i> | 2022 | 2021 |
| Revenue: | | |
| Parent (c) | 74,768 | 8,590 |
| Other related parties | 416,495 | 58,556 |
| Power purchased: | | |
| Other related parties (d) | 5,893 | 3,957 |
| Operating costs: | | |
| Parent | 6,242 | 5,874 |
| Transmission expense: | | |
| Other related parties | 118,305 | 136,079 |
| Other expense: | | |
| The Province | 12,512 | 2,660 |
| Other related parties | (903) | - |

(a) Muskrat Falls has a related party loan receivable with Labrador Transco which includes interest charged at 5.43% and is payable from Labrador Transco as cash becomes available while still meeting its debt servicing costs.

MUSKRAT FALLS CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

- (b) Muskrat Falls has a related party loan payable with Hydro which includes interest charged at 5.43% and is payable from Muskrat Falls as cash becomes available while still meeting its debt servicing costs.
- (c) Muskrat Falls has contributed energy to Nalcor related to delivery of the Nova Scotia Block.
- (d) Muskrat Falls has a contribution of power purchases from Nalcor related to delivery of the Nova Scotia Block.

18. COMMITMENTS AND CONTINGENCIES

- (a) Muskrat Falls has entered into the GIA and PPA with Labrador Transco and Hydro, for an expected term of 57 years, whereby Muskrat Falls has committed to design, construct, operate and maintain the MF Plant, and provide such other services as agreed to ensure safe and reliable transmission of electricity. Revenue allocated to the remaining performance obligation (unsatisfied or partially unsatisfied) related to energy and capacity sales under the PPA as at December 31, 2022 total \$544.4 million within one year and \$37,030.3 million in more than one year.
- (b) As part of the MF/LTA PFA, Muskrat Falls has pledged its present and future assets as security to the Collateral Agent.
- (c) In July 2012 Nalcor entered into the Energy and Capacity Agreement with Emera Inc. (Emera) providing for the sale and delivery of the Nova Scotia Block, being 0.986 TWh of energy annually for a term of 35 years. In October 2015 Nalcor assigned this agreement to Muskrat Falls. As a result of this assignment, Nalcor and Muskrat Falls are jointly liable for the delivery of the Nova Scotia Block to Emera.
- (d) The Water Management Agreement between Churchill Falls and Muskrat Falls provides for coordinated production for the efficient use of water on the Churchill River system by ensuring that water is available to meet delivery requirements and contractual commitments for both Churchill Falls and Muskrat Falls, while maximizing the energy produced from the water resource. As at December 31, 2022 Muskrat Falls has the equivalent of approximately 1.5 Twh (2021 – 1.3 Twh) of energy stored in the Churchill Falls reservoir.
- (e) Muskrat Falls is subject to legal claims with respect to construction and other various matters. For some legal claims, it is not possible at this time to predict with any certainty the outcome of such litigation. Should these claims result in an unfavourable outcome for the Company, they may have a significant adverse effect on the Company's financial position.
- (f) Outstanding commitments for capital projects total approximately \$7.4 million as at December 31, 2022 (2021 - \$23.6 million).

19. CAPITAL MANAGEMENT

Capital includes share capital, shareholder contributions and long-term debt. The Company's objectives for managing capital are to maintain its ability to continue as a going concern and to ensure timely payment of its contractual obligations. Cash generated from operations will be sufficient to fund the operating, maintaining and sustaining activities of the MF Plant.

MUSKRAT FALLS CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

20. SUPPLEMENTARY CASH FLOW INFORMATION

| <i>For the year ended December 31 (thousands of Canadian dollars)</i> | 2022 | 2021 |
|---|------------------|----------|
| Trade and other receivables | (21,082) | 843 |
| Prepayments | 297 | 2,521 |
| Inventories | (571) | (34) |
| Trade and other payables | (100,970) | 918 |
| Changes in non-cash working capital balances | (122,326) | 4,248 |
| Related to: | | |
| Operating activities | (7,804) | 17,889 |
| Investing activities | (114,522) | (13,641) |
| | (122,326) | 4,248 |