# NEWFOUNDLAND AND LABRADOR HYDRO

2019 Annual Performance Report
Transparency and Accountability

September 2020

newfoundland labrador hydro
a nalcor energy company

## Message from the Board of Directors

In accordance with the **Transparency and Accountability Act***,* I am pleased to provide the 2019 Annual Performance Report for Newfoundland and Labrador Hydro (Hydro), on behalf of the Board of Directors.

The 2017-2019 Strategic Plan for Hydro outlined how the corporation would address the applicable strategic directions of the Provincial Government in relation to Hydro's role in the energy sector as communicated by the Minister of Industry, Energy and Technology.

As the Board of Directors of Hydro, we are accountable for the preparation of this report and are accountable for the results.

John Green, QC
Chair
Newfoundland and Labrador Hydro

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# 1. Overview

As the main generator and transmitter of electricity for use in the province, Newfoundland and Labrador Hydro (Hydro) is focused on providing a safe, reliable and least-cost electricity supply to meet current energy demand and future growth of its customers. Hydro is a wholly owned subsidiary of Nalcor.

The majority of Hydro's business is regulated by the Newfoundland and Labrador Board of Commissioners of Public Utilities (PUB) and its electricity rates are set through periodic general rate applications. The regulated portion of the company includes the generation, transmission and distribution of electrical power and energy to utility, residential and commercial customers, as well as island industrial customers. The non-regulated activities of Hydro include electricity sales to industrial customers in Labrador west.

Hydro's electricity production assets include nine hydroelectric plants, one oil-fired plant, four gas turbines, and 24 diesel plants[1]. These assets along with a network of transmission and distribution lines bring electricity to communities throughout Newfoundland and Labrador (see Appendix 1).

Hydro also holds a 65.8 per cent interest in Churchill Falls (Labrador) Corporation Limited. The operations of Churchill Falls are managed by Nalcor's Power Supply division and included in the 2017-2019 Nalcor Strategic Plan and 2019 Nalcor Annual Performance Report.

## *Mandate*

The **Hydro Corporation Act, 2007** mandates Hydro to be responsible for:

- Developing and purchasing power and energy on an economic and efficient basis.

[1] With the relocation of the town of Little Bay Islands on December 31, 2019, the diesel plant in the community ceased operations.

- Engaging within the province and elsewhere in the development, generation, production, transmission, distribution, delivery, supply, sale, purchase and use of power from water, steam, gas, coal, oil, wind, hydrogen and other products.
- Supplying power, at rates consistent with sound financial administration, for domestic, commercial, industrial or other uses in the province and subject to the prior approval of the Lieutenant-Governor in Council, outside of the province.

### *Lines of Business*

Hydro delivers power to utility, industrial, residential and commercial customers in more than 200 communities in the province at the lowest possible cost consistent with reliable service. Hydro activities can be grouped as follows:

- Electricity production – Hydro has an installed generating capacity of 1,763 megawatts (MW) which includes the operations of nine hydroelectric generating stations, one oil-fired plant, four gas turbines, and 24 diesel plants[2], including 19 isolated diesel generating and distribution systems.
- Transmission and distribution – Hydro operates and maintains over 4,400 kilometres of transmission lines and 69 terminal stations which connect to generation and delivery points for Newfoundland Power on the island, industrial customers, and Hydro's rural distribution systems province-wide. Hydro also operates and maintains approximately 2,700 kilometres of distribution lines throughout the province.
- The Newfoundland and Labrador System Operator (NLSO) acts as the independent operator to manage the provincial electricity system in real-time. The NLSO also provides open access to the provincial transmission network, which means providing transmission service to users like Hydro and other qualified customers, in an open, non-discriminatory and non-preferential manner.
- Customer service activities address the electricity requirements of Newfoundland Power, industrial customers and over 38,800 direct residential and commercial

[2] With the relocation of the town of Little Bay Islands on December 31, 2019, the diesel plant in the community ceased operations.

customers in rural Newfoundland and Labrador.

- Electricity system planning involves forecasting short and long-term electricity requirements in the province and advancing options to ensure adequate supply of generation resources and transmission and distribution infrastructure to reliably meet forecasted demand. Planning for supply adequacy requires the critically important activities of oversight of fuel and water management

### *Values*

Employees of Hydro recognize that electricity is essential to social well-being and economic prosperity in Newfoundland and Labrador. In fulfilling Hydro's mandate, employees are unified by the following core values:

- Safety – relentless commitment to protecting ourselves, our colleagues, and our community.
- Open Communication – fostering an environment where information moves freely in a timely manner.
- Accountability – holding ourselves responsible for our actions and performance.
- Honesty and Trust – being sincere in everything we say and do.
- Teamwork – sharing our ideas in an open and supportive manner to achieve excellence.
- Respect and Dignity – appreciating the individuality of others by our words and actions.
- Leadership – empowering individuals to help guide and inspire others.

### *Primary Clients*

Hydro sells electricity to three primary customer groups:

- Newfoundland Power - an investor-owned utility which distributes electrical power to 268,000 customers on the island portion of the province, with Hydro supplying over 90 per cent of its energy requirements.
- Industrial customers – On the Island, regulated sales to NARL Refining Limited Partnership, Vale Newfoundland and Labrador, Praxair Canada Inc., Teck Resources Limited, and Corner Brook Pulp and Paper Limited. In Labrador, regulated transmission

service and unregulated generation service to the Iron Ore Company of Canada and Tacora Resources Incorporated.

- Over 38,800 residential and commercial customers in rural Newfoundland and Labrador.

### *Vision*

Providing electricity to enable social well-being and economic prosperity for the people of Newfoundland and Labrador.

### *Number of Employees, Physical Location and Other Key Statistics*

Headquartered in St. John's with assets and offices throughout the province, Hydro directly employed 925 people in permanent, term and temporary capacities as of December 31, 2019[3]. The location of these employees reflects Hydro's service area and the location of the company's electricity assets, with 66 per cent located in rural areas. The gender composition of Hydro's employee group is 78 per cent male and 22 per cent female. In 2019, Hydro advanced its commitment to diversity and inclusion and hired 12 of 33 (36 per cent) new hire apprentices, co-operative education students and graduate engineers from under-represented groups including 10 women. In addition, 10 of the 40 (25 per cent) new managers, supervisors and engineers hired were women.

| Gender | Rural | Urban | Total | Per cent |
|---|---|---|---|---|
| Female | 70 | 132 | 202 | 22% |
| Male | 539 | 184 | 723 | 78% |
| **Total** | 609 | 316 | 925 | |
| **Per cent** | 66% | 34% | | |

[3] This is the number of employees on payroll for the last pay period of 2019, it is not full-time equivalents. This approach supports the analysis of employee location and gender required.

## *Board of Directors*

As of December 31, 2019, the Hydro Board of Directors comprised:

- John Green, QC (Chair)
- Donna Brewer
- Fraser H. Edison
- Chris Loomis
- John Mallam
- Stan Marshall
- William Nippard
- David Oake
- Brendan Paddick
- Brian Walsh

## *2019 Consolidated Revenues and Expenses*

In 2019, Hydro had revenues of $748 million. The majority of Hydro's revenues are from regulated energy sales to utility, rural and industrial customers with other revenues including preferred dividends from Hydro's subsidiary Churchill Falls. Consolidated energy sales also include Hydro's share of Churchill Falls sales to Hydro Québec as well as sales of recall power. In 2019, Hydro net income of $63 million consisted of $30 million from Hydro Regulated, $35 million from Churchill Falls, $1 million from activities associated with energy marketing for Hydro, and a loss of $3 million from non-regulated activities. The following table summarizes the 2019 consolidated revenue and expenses for Hydro:

| *For the year ended December 31 (millions of dollars)* | ($) | % |
|---|---|---|
| Energy sales | 720 | 96.3 |
| Other revenue | 28 | 3.7 |
| **Revenue** | **748** | |
| Fuels | 217 | 30.1 |
| Power purchased | 99 | 13.7 |
| Operating costs | 184 | 25.5 |
| Transmission rental | 22 | 3.0 |
| Depreciation and amortization | 103 | 14.3 |
| Net finance expense | 89 | 12.3 |
| Other expense | 8 | 1.1 |
| **Expenses** | **722** | |
| **Profit before regulatory adjustments** | **26** | |
| Regulatory adjustments | (37) | |
| **Profit for the year** | **63** | |

The 2019 Consolidated Financial Statements for Hydro are appended to this document (see Appendix 2).

## 2. Highlights and Partnerships

Hydro works with a variety of agencies, departments and commissions to execute its mandate. During the planning period, Hydro worked closely with each of these organizations to advance its mandate in the electricity sector in support of the strategic directions of the Provincial Government.

### *Department of Industry, Energy and Technology*

The Department of Industry, Energy and Technology (formerly the Department of Natural Resources) works with Hydro in policy-related areas for the electricity sector. In 2017-2019 planning period, Hydro worked with the Department and Nalcor to identify and evaluate options to mitigate projected customer rate increases associated with the Muskrat Falls Project and assess responses to potential new industrial customers. Hydro also provided input to amendments to the **Public Utilities Act,** 1994 and the **Electrical Power Control Act** required for open access[4] to the provincial electricity transmission system, including the establishment of the NLSO to administer open access. During the planning period Hydro supported the efforts of the Department to progress consideration of renewable generation options for remote communities. In 2019, Hydro also worked with the Department to advance electricity sector priorities including electric vehicle charging infrastructure to facilitate the increased use of electric vehicles. Hydro also has frequent discussions with the Department in the provision of information related to electricity rates and the Department is copied on all applications filed with the PUB. On behalf of the Department, Hydro also delivers the Northern Strategic Plan rebate to residential customers in isolated diesel systems in Labrador through a monthly credit on their electricity bills.[5]

[4] The open access transmission regime provides open, non-discriminatory and non-preferential access to service on the province's high-voltage electricity transmission system. It is an important component of broadening participation in both import and export electricity markets.

[5] This rebate is funded by the Provincial Government and is not included in the PUB-approved rates. The rebate brings the costs of the monthly Basic Customer Charge and lifeline block of energy for Labrador rural isolated diesel and Labrador Straits residential electricity customers in line with comparable Happy Valley – Goose Bay residential electricity costs. It is intended to provide some rate assistance to residential customers.

### *Newfoundland and Labrador Board of Commissioners of Public Utilities (PUB)*

The PUB is responsible for regulatory oversight of Hydro's regulated utility activities. This responsibility covers a wide range of activities, including approval of its revenue requirements and the allocation of the revenue requirements among customer classes, rates, rate structure, customer contribution policies, long term debt financing, system planning criteria and, the capital program. The role of the PUB is detailed in the **Public Utilities Act**.

During 2017-2019 period there was significant regulatory activity related to the 2017 General Rate Application including public hearings and settlement negotiations. There were also significant other filings related to the study of electricity supply adequacy for the Island Interconnected System and the necessity of transmission investments to provide reliable supply to meet customer load requirements on the Labrador Interconnected System. In 2018 and 2019, Hydro also participated in the PUB reference for Rate Mitigation Options and Impacts Relating to the Muskrat Falls Project Costs[6]. Other regulatory activity during the planning period included Hydro's annual capital budget application, a regulatory process on the cost of service methodology to apply in determining customer rates after the commissioning of the Muskrat Falls Project, as well as significant ongoing reporting.

### *Department of Finance*

The Department of Finance works with Hydro to address requirements related to financial policy including capital structure, dividend policy and legislative debt caps as well as the corporation's debt financing activities. During 2017-2019 period, Hydro changed the method by which it issued long term debt. In 2017, $300M of long term debt was issued directly in capital markets with a Provincial Guarantee. Hydro then changed the method by which it issues long term debt to on in which the Province issues debt specifically on Hydro's behalf and

On September 5, 2018, the Government of Newfoundland and Labrador released the terms of reference for Rate Mitigation Options and Impacts Relating to the Muskrat Falls Project Costs. The PUB was requested to consider a series of questions and lead a process to gather information and make recommendations to the Government.

lends those proceeds directly to Hydro. This new method was used to issue a total of $600M of long term debt in 2017 and 2018.

### *Other Departments/Public Bodies*

Hydro interacts with the Departments of Environment, Climate Change and Municipalities (formerly Municipal Affairs and Environment), Fisheries, Forestry and Agriculture (formerly Fisheries and Land Resources), Tourism, Culture, Arts and Recreation (formerly Tourism, Culture, Industry and Innovation), Intergovernmental and Indigenous Affairs, and Digital Government and Service NL (formerly Service NL) in relation to environmental aspects of the corporation's activities. For example, Hydro interacted with the Department of Environment, Climate Change and Municipalities on the air emissions and greenhouse gas files, watercourse crossings associated with operation and maintenance of transmission line corridors, variance requests associated with fuel storage tank systems and reviewing Hydro's integrated vegetation management program. Hydro also managed the Heat Pump Rebate Program, the Energy Efficiency in Oil Heated Home Program and the 3-year Energy Efficiency Loan Program on behalf of the Environment, Climate Change and Municipalities. Environmental Assessment Division and Natural Areas were engaged in the hiring process associated with independent monitors required during post construction associated with transmission line 267. Intergovernmental and Indigenous Affairs were consulted for work requiring environmental approvals in Labrador. Hydro also engaged with Environmental Assessment division in the registration of two projects (Petite Forte distribution line upgrade and the Springdale terminal station flood control berm).

## 3. Issues

The strategic issues outlined below will be addressed by Hydro in order to realize its mandate and vision. Consistent with the underlying philosophy of the multi-year performance-based planning required under the provisions of *Transparency and Accountability Act,* these issues are at a governance level and reflect the priorities of the Hydro board and support the Provincial Government's strategic directions for the electricity sector.

Issue 1: Reliable electricity supply

Issue 2: Electricity rates and customer service

Issue 3: Safety

# 4. Outcomes

## ISSUE 1: RELIABLE ELECTRICITY SUPPLY

Hydro ensures there is a safe, reliable and least-cost electricity supply available to meet the needs of customers now and in the future. The company's mandate supports fulfillment of the strategic direction of government related to energy security and reliability in Newfoundland and Labrador.

During the planning period, Hydro focused on providing a reliable electricity supply by maintaining and renewing assets, preparing for the interconnection between Labrador and the Island via the Labrador Island Link, as well as developing new operating and planning parameters and continuing to assess how to meet future customer requirements.

Maintaining Hydro's systems in reliable operating condition is accomplished through a combination of planned maintenance, rehabilitation of existing assets, and replacement of assets that have reached the end of their useful lives. Replacement of assets may also occur to lower life cycle costs, improve operational characteristics, increase capacity for load growth, correct reliability criteria violations, improve productivity, or increase efficiency.

The majority of Hydro's installed assets, including the hydroelectric facility at Bay d'Espoir, the Holyrood Thermal Generating Station ("Holyrood TGS"), the Stephenville Gas Turbine, the Hardwoods Gas Turbine, and much of Hydro's transmission and distribution systems, are more than 40–50 years old.

From 2005-2019, Hydro invested in excess of $1.5 billion to expand, upgrade or replace its assets. In 2019, Hydro invested $126.6 million for the execution of capital projects to contribute to the provision of safe, reliable, least-cost electricity to customers.

The provincial electricity system is changing with the development of the Muskrat Falls generation project and associated transmission facilities including interconnection to the North American electricity grid through the Maritime link and to Labrador through the Labrador-Island Link. Planning and preparing for these changes present an opportunity to reliably meet the needs of customers in the future.

Over the planning period, Hydro completed critical activities related to the inter-provincial flow of electricity and the integration of Muskrat Falls power and assets. In 2018, over 50 gigawatt hours (GWh)[7] was imported over the Maritime Link to displace more costly thermal generation and over 53 GWh of low cost recapture energy from Churchill Falls was delivered to the island during Labrador Island Link commissioning activities in 2018 displacing an equivalent amount of thermal generation. In 2019, some 244.5 GWh was imported over the Maritime Link and over 214.6 GWh of recapture energy from Churchill Falls was delivered to the island during Labrador Island Link commissioning activities, displacing an equivalent amount of thermal generation. In addition to savings related to fuel costs, the electricity system changes associated with the Maritime Link prevented customer reliability from being impacted by 11 system events in 2018 and an additional 23 events in 2019. The majority of these system events were not system equipment interruptions but related to new asset testing, which was expected.

Hydro has a responsibility to assess electricity requirements in the province and identify options to meet future growth in customer requirements. In 2018, Hydro completed a Reliability and Resource Adequacy Study to address the long-term approach to providing least-cost reliable electricity service; Hydro updated this study in 2019. This study also documented how Hydro evolved its legacy planning processes to address previous gaps as identified in external assessments. To further inform this study and its resultant investment decisions, Hydro developed and completed its first ever plan to engage directly with customers to get their views on the balancing reliability and cost. This type of engagement will continue in the coming

[7] Gigawatt hours (GWh) is a unit of energy representing one billion (1 000 000 000) watt hours and is equivalent to one million kilowatt hours.

planning period. Hydro will participate in the PUB review of these studies and will develop an implementation plan based on the direction received from the regulator.

Hydro also continued to assess electricity requirements and options to respond in the Labrador Interconnected System and isolated diesel communities during the planning period. Hydro worked with potential new industrial and data mining companies seeking possible service in Labrador West, Churchill Falls and Happy Valley-Goose Bay as well.

| **ISSUE 1: RELIABLE ELECTRICITY SUPPLY** | |
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| **Goal**<br>By December 31, 2019, Hydro will have advanced initiatives to support electricity system reliability. | |
| INDICATORS | 2017-2019 ACCOMPLISHMENTS |
| Developed reliability improvement plans for key generating and transmission assets and supporting infrastructure. | During the 2017-2019 planning period, Hydro developed annual reliability improvement plans. These plans outlined initiatives to improve the reliability of Hydro's generating plants, transmission and distribution lines, and terminal stations. In addition to improving maintenance and equipment installation and replacement, reliability improvement plans also included training activities to enhance employee technical knowledge.<br><br>For each year of the planning period, completion of initiatives outlined in the annual reliability improvement plans was greater than the 90 per cent completion rate target. |
| Completed required maintenance work and capital investments to support reliability. | Hydro also developed integrated annual work plans documenting required maintenance work and capital investments for each year of the planning period.<br><br>For each year of the planning period, completion of initiatives outlined in the integrated annual work plans was greater than the 90 per cent completion rate target. |
| Assessed the adequacy of future electricity supply and identified options to address any issues. | During the planning period Hydro continued to analyse electricity supply requirements and report to the PUB. Hydro's revised approach to electricity supply planning was a major shift from legacy planning processes.<br><br>In 2017, Hydro filed the Near-term Generation Adequacy Report with the PUB. The Report concluded that based on |

| **ISSUE 1: RELIABLE ELECTRICITY SUPPLY** | |
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| | asset reliability and in consideration of its energy in storage, Hydro would be able to meet Island Interconnected System customer electricity requirements.<br><br>In 2018, Hydro filed the 2018 Reliability and Resource Adequacy Study with the regulator. The 2018 study took into consideration Hydro's current and future electricity supply, changing sources of supply, electricity load forecasts and electricity system risks. As part of this process, Hydro launched ElectricityFeedbackNL.com as an easy way for electricity customers to share their input and opinions about the future of electricity in Newfoundland and Labrador. The feedback was included in the report filed with the regulator. Reflecting the evolution of Hydro's planning processes, the study included recommendations regarding modifications to planning criteria and the extension of the system energy planning criteria to the entire Provincial Interconnected System.<br><br>In 2019, Hydro completed its annual update to the Reliability and Resource Adequacy Study. The 2019 update addressed requirements of the Board identified in correspondence to Hydro as well as the recommendations of the Board's consultant arising from its review of the 2018 Reliability and Resource Adequacy filing. The update provided additional detail on matters Hydro continued to investigate through 2019 and responded to the recommendations detailed in a review of the 2018 filing completed by a consultant for the Board. The regulatory review of the Study will continue in 2020 |
| Advanced preparations for interconnection of electricity systems and integration of Muskrat Falls power and assets. | During the 2017-2019 planning period, Hydro completed critical activities related to the inter-provincial flow of electricity and the integration of Muskrat Falls power and assets. These activities related to the electricity system studies, negotiation of commercial arrangements, putting operational processes in place, and regulatory activities. Key accomplishments that were enabled by Hydro's support included:<br>▪ Completed studies on how electricity system performance will change as new assets are integrated, and developed procedures to enable optimal use of these assets while ensuring reliable operation throughout their integration.<br>▪ Implemented framework to provide transmission customers with open access to the provincial transmission |

| **ISSUE 1: RELIABLE ELECTRICITY SUPPLY** | |
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| | system, including establishment of the Newfoundland and Labrador System Operator (NLSO) to administer open access, PUB approval of interim transmission tariff, and Hydro's execution of Transmission Service Agreements for use of the system in accordance with the new framework.<br>▪ Supported commissioning of the Maritime Link resulting in improved reliability and greater flexibility of operations on the Island Interconnected System.<br>▪ Executed Power Purchase Agreement with Nalcor Energy Marketing to provide for imports over the Maritime Link, and amended existing agreements to enable use of recapture energy on the island.<br>▪ Executed Interim Transmission Funding Agreements and Minimum Performance Guarantee for the Labrador Island Link and Labrador Transmission Assets to have the assets put into limited service in advance of full commissioning of the Labrador Island Link and the Muskrat Falls generation station.<br>▪ Executed and obtained PUB approval of the Pilot Agreement for Optimization of Hydraulic Resources to enable the use of Hydro's assets to gain value from external markets.<br>▪ Initiated development of a commercial compliance framework to ensure appropriate awareness and accountability within Hydro of obligations contained in key commercial agreements. |
| **Objective**<br>By December 31, 2019, Hydro will have further advanced investments and initiatives to enhance electricity system reliability. | |
| INDICATORS | 2019 ACCOMPLISHMENTS |
| Developed annual reliability improvement plans for key generating and transmission assets and completed priority activities. | In 2019, reliability improvement plans were developed identifying nearly 300 actions with a target completion rate of 90 per cent. At year-end, priority actions, and overall 93 per cent of actions, were completed as planned.<br><br>Reliability improvement plans included initiatives to improve the reliability of Hydro's generation, transmission, terminal station and distribution assets. Plans addressed improving employee technical and process knowledge, improving effectiveness of asset management system processes and improving equipment installation, assessment, maintenance and replacement practices. |

| **ISSUE 1: RELIABLE ELECTRICITY SUPPLY** | |
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| Completed required maintenance activities and capital projects to support readiness for the 2019/20 winter season. | All winter readiness work (100 per cent) for the Holyrood Thermal Generating Station and on the transmission system was completed by the December 1 target date. Overall, Hydro completed 99.9 per cent of winter readiness activities by this date.<br><br>Two pieces of planned work were not completed. The planned inspection of a generating unit at Bay d'Espoir that occurs every six years and requires a five week outage was not completed as planned. Due to a compressed unit outage window, Hydro instead completed an annual inspection as well as corrective maintenance activities required to ensure the reliability of the generating unit for the 2019-2020 winter. Hydro considers the deferral of the original inspection scope to 2020 as low risk.<br><br>The second winter readiness activity not completed was the refurbishment of the spare engine for Hardwoods and Stephenville gas turbines. Considerable work was completed on this activity but multiple issues with spare engines resulted in delays. The spare gas turbine engine for Stephenville and Hardwoods gas turbines was received in early 2020. |
| Completed planned 2019 capital investments | In 2019, Hydro invested $126.6 million in capital to renew electricity generation and transmission assets. This included:<br>▪ $21.2 million spent on hydraulic generation equipment and infrastructure across the province with $2.6 million to refurbish powerhouse station services in Bay d'Espoir and $8.9 million for year one in the Hydraulic Generation Refurbishment and Modernization (2019– 2020) project.<br>▪ $8.7 million for thermal generation equipment and infrastructure at the Holyrood Thermal Generating Station.<br>▪ $6.4 million for gas turbines, over half of which ($3.6 million) related to increasing fuel and water treatment system capacity at the Holyrood Gas Turbine.<br>▪ Sustaining capital for terminal station infrastructure totalled $31.1 million, including $7.9 million to upgrade circuit breakers and $9.6 million to refurbish and modernize terminal stations.<br>▪ In transmission, $2.9 million was invested through the Wood Pole Line Management Program.<br>Actual 2019 expenditures were $37.6 million (22.9 per cent) lower than the budget of $164.2 million. The three main drivers |

| **ISSUE 1: RELIABLE ELECTRICITY SUPPLY** | |
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| | of the lower than budgeted expenditures were: 1) some of the project work scopes were completed for less than the budget estimates; 2) some project work scopes could not be completed in 2019 because equipment outages were not available, resulting in planned expenditures being deferred to 2020; and 3) some project work scopes were cancelled as they were no longer required. |
| Participated in regulatory review of the 2018 Reliability and Resource Adequacy Study as required, and completed 2019 update to assess electricity supply adequacy for the Island Interconnected System (IIS). | Hydro completed a 2019 update to the 2018 Reliability and Resource Adequacy Study and filed the update with the Board on November 15, 2019.<br><br>As previously noted, the 2019 update addressed requirements of the Board arising from its review of the 2018 Reliability and Resource Adequacy filing. The regulatory review of the Study will continue in 2020. |
| Supported the regulatory review of the Labrador West Transmission Planning Study as required, and developed required capital budgets as part of the 2020 Capital Budget Application to the PUB. | In 2018 Hydro completed the Labrador Interconnected System Transmission Expansion Study and filed the results with the PUB. The study included consideration for a range of load forecasts with the objective of identifying least-cost, reliable electricity transmission system additions required for both eastern and western Labrador.<br><br>In 2019, Hydro completed additional studies to support the review of short-term Labrador transmission supply options as well as forecasted load. Capital budgets were not required as part of the 2020 Capital Budget Application to the PUB however several projects to add capacity are being proposed as part of the 2021 Capital Budget Application. |
| Completed critical activities related to the integration of Muskrat Falls power and assets. | In 2019, Hydro completed critical activities related to inter-provincial flow of electricity and the integration of Muskrat Falls power and assets. These activities included<br>▪ Identified and assessed potential commercial arrangements to enable Nalcor to fulfil obligations made to Nova Scotia in relation to the Lower Churchill Project.<br>▪ Agreed on principles of a long term marketing and optimization agreement with Nalcor Energy Marketing and the Muskrat Falls Corporation, and a mature draft is continuing to be advanced.<br>▪ Developed and implemented operating strategies to maximize deliveries over the Labrador Island Link to displace higher cost production from Holyrood.<br>▪ Contingency planning for Muskrat Falls Plant commissioning |

| **ISSUE 1: RELIABLE ELECTRICITY SUPPLY** | |
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| | and operations without the Labrador Island Link is ongoing, and the associated commercial framework is well advanced.<br>▪ NLSO requirements for the Labrador Transmission Assets were met, and operational control was transferred to NLSO.<br>▪ Point to Point Transmission Service Agreement for exports executed between Hydro and NLSO.<br>▪ Commercial compliance program development initiated; checklists for highest priority agreements complete, individual owners for integration related contracts identified and approved.<br>▪ Developed scheduling protocol for Muskrat Falls generation, as required under the Muskrat Falls Power Purchase Agreement. |

## ISSUE 2: ELECTRICITY RATES AND CUSTOMER SERVICE

As the primary generator of electricity in the province, Hydro has a significant impact on social well-being and economic prosperity in the province. In fulfilling its mandate, Hydro supports the strategic direction of the Provincial Government regarding maximized value and more specifically the focus to minimize the burden on electricity customers in the province. This section of the report outlines Hydro progress related to electricity rates as well as customer service and energy efficiency activities.

Electricity rates are impacted by a number of factors including capital investments in the electricity system, power purchase costs, fuel costs and the overall cost of operations. Hydro's mandate requires a commitment to the provision of least-cost power to customers in Newfoundland and Labrador. This commitment is reflected in a prudent approach to capital investment that ensures the appropriate balance between cost and reliability and a focus on completing the required maintenance of assets while managing operating costs.

A key driver of future electricity rates is the cost of the Muskrat Falls project. During the planning period, Hydro worked with its parent company Nalcor through the Rate Mitigation Steering Committee chaired by Government of Newfoundland and Labrador to determine potential options to mitigate and manage these cost increases for customers. Initiatives implemented or advanced arising from this committee include the commencement of a cross island electric vehicle charging network and advancement of public building conversions from oil heat to electric heat, both projects which will enable increased domestic energy usage. Additionally, Hydro worked with government on Expressions of Interest related to diesel offset in rural communities.

On September 5, 2018, the Government released the terms of reference for Rate Mitigation Options and Impacts Relating to the Muskrat Falls Project Costs. The PUB was requested to

consider options to reduce the impact of Muskrat Falls Project costs on electricity rates; the amount of energy and capacity from the Muskrat Falls Project required to meet Island interconnected load and the remaining surplus energy and capacity available for other uses such as export and load growth; and, potential electricity rate impacts of the options identified based on the most recent Muskrat Falls Project cost estimates.

Hydro provided input to the PUB process in 2018 and 2019. In September 2019, Hydro outlined an Efficiency and Effectiveness Plan in evidence and committed to achieve savings in the range of $2 million through efficiencies and productivity gains. Hydro also committed to undertaking a multi-year review of the Exploits operations, targeting annual savings of $2.5 million, subject to the degree of employee dislocation that is able to be attained.

Hydro recognizes the need to balance system investment to maintain reliability with the management of cost to minimize upward pressure on customer rates. During each annual Capital Budget Application, Hydro refines its next five-year capital plan. In the 2020 plan, developed in 2019, Hydro reduced its capital investment plans where prudent and where Hydro would not be placing the system at inappropriate risk; no priority work activities or projects were deferred.

Hydro delivers the majority of the electricity needed by Newfoundland Power to address their customers' needs and also directly serves over 38,800 residential and commercial customers and several large industrial customers. Hydro's commitment to customers also includes education and programs to help customers reduce their electricity use and costs. In the 2017-2019 planning period, Hydro continued efforts to help residential, commercial and industrial electricity consumers conserve energy.

| **ISSUE 2: ELECTRICITY RATES AND CUSTOMER SERVICE** | |
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| **Goal**<br>By December 31, 2019, Hydro will have supported measures to mitigate electricity rate increases and advanced customer service and energy efficiency initiatives. | |
| INDICATORS | 2017-2019 ACCOMPLISHMENTS |
| Identified and implemented measures to manage operating and capital costs. | Hydro cost management efforts focus primarily on the significant components of operating and maintenance costs including labour related costs (e.g. salaries, benefits, overtime), and system equipment maintenance.<br><br>In 2017, actual operating costs of $130.1 million were $8.5 million below budget and in 2018, operating costs of $136.0 million were $8.1 million below budget. Again in 2019, cost management efforts and the capitalization of work previously budgeted as maintenance resulted in operating and maintenance costs of $133.1 million versus the approved budget of $136 million.<br><br>Hydro recognizes the need to balance electricity system investment to maintain reliability with the management of cost to minimize upward pressure on customer rates. In the 2020 Capital Budget Application filed with the PUB in 2019, Hydro realigned projects based on condition of assets and in some instances projects are included in later times than previously assessed to better balance capital investments with customer expectations for cost management and reliability. The review of 2020 capital budget resulted in the reduction of planned capital expenditures from $133.6 million to $111.9 million.[8] |
| Supported assessment and implementation of measures to mitigate the impact of the Muskrat Falls costs on rates. | During the planning period Hydro supported efforts to identify and assess measures to mitigate the impact of Muskrat Falls costs on electricity rates in the province.<br><br>In 2017, a Rate Mitigation Steering Committee chaired by the Department of Industry, Energy and Technology with representatives from the Department of Finance, Nalcor and Hydro was formed. Over the planning period, Hydro |

[8] The 2020 Capital Budget Application to the PUB includes a planned total value of $111,947,300 however, the 2020 CBA only seeks approval of $108,487,300 and excludes 2019-2022 Additions for Load – Increase Capacity in Labrador West Project ($3,460,000 in 2020). Additional technical analysis is required for the project and a supplemental application will be prepared. The 2020 Capital Budget application was approved by the PUB on February 21,2020 [P.U. 6 (2020)].

| ISSUE 2: ELECTRICITY RATES AND CUSTOMER SERVICE | |
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| | participated in the Committee.<br><br>In September 2018, the Government of Newfoundland and Labrador released the terms of reference for Rate Mitigation Options and Impacts Relating to the Muskrat Falls Project Costs. The PUB was requested to consider a series of questions (the Reference) related to options to reduce the impact of Muskrat Falls Project Costs on electricity rates. Hydro and Nalcor supported the efforts of the PUB and it's consultants throughout 2018 and 2019 and presented evidence in the fall of 2019. Hydro committed to achieving savings in the range of $2 million through efficiencies and productivity gains. Hydro also committed to undertaking a review of Exploits operations, targeting annual savings of $2.5 million, subject to the degree of employee dislocation that is able to be attained.<br><br>In April 2019, Government of Newfoundland and Labrador released **Protecting You from the Cost Impacts of Muskrat Falls**. Hydro has been supporting the efforts of government related to several initiatives outlined in this strategy. These initiatives include raising revenue by adding value to the energy surplus available from the Muskrat Falls Project and Holyrood performance credits awarded for greenhouse gas reductions. |
| Evaluated customer satisfaction and developed and implemented initiatives to enhance customer service. | Hydro completed commercial customer satisfaction assessment in 2017 and again in 2019 and measured residential customer satisfaction in 2018.<br><br>Over the planning period, Hydro completed initiatives to enhance customer service including the implementation of the MyNLHydro customer self serve option. This option responds to customer feedback requesting more convenient ways of interacting with Hydro. Also, based on commercial customers' requests for greater information and consultation around outages, Hydro has included this in its outage planning process.<br><br>*Commercial Customer Satisfaction*<br>In 2019, 83 per cent of commercial customers were either very or somewhat satisfied with Hydro. This is fairly consistent with 2017 results when 85 per cent of commercial customers were either very or somewhat satisfied with Hydro. In both years, |

**ISSUE 2: ELECTRICITY RATES AND CUSTOMER SERVICE**

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| | customers expressed satisfaction with reliability, and overall customer service.<br><br>*Residential Customer Satisfaction*<br>In 2018, the vast majority of residential customers remain satisfied with Hydro resulting in an 89 per cent overall satisfaction rating. The survey indicated that 47 per cent of residential customers are very satisfied and 42 per cent are somewhat satisfied. When compared to the overall satisfaction rating of 90 per cent in 2016, Hydro has remained relatively consistent. |
| Promoted energy conservation by residential, commercial and industrial customers. | Hydro delivered energy efficiency programs to residential and commercial customers during the 2017-2019 planning period. These programs included the joint utility programs through takeCHARGE delivered in partnership with Newfoundland Power as well as Hydro's energy efficiency programs. Hydro also supported the delivery of government sponsored energy efficiency programs. |

Table 1: Summary of Energy Conservation Programs 2017-2019

| Program | 2017 | 2018 | 2019 | Total |
|---|---|---|---|---|
| takeCHARGE | | | | |
| - Residential customer rebates (insulation upgrades, thermostats, heat recovery ventilators, and appliances) | 173 | 135 | 86 | 394 |
| - Commercial customer rebates (energy efficient technologies) | 39 | 26 | 10 | 75 |
| - Energy Efficiency Loan Program | 33 | 28 | 11 | 72 |
| Isolated Systems Community Energy Efficiency Program | | | | |
| - Residential and commercial customers assisted (number) | 1,007 | 727 | 1,160 | 2,894 |
| - Annual energy savings (MWh) | 1,141 | 1,064 | 1,197 | 3,402 |
| Business Efficiency Program | | | | |
| - Facility audits (number) | 46 | 34 | 13 | 93 |
| - Annual energy savings from projects and rebates (MWh) | 908 | 430 | 234 | 1,572 |
| Industrial Customers | | | | |
| - Industrial customer projects (number) | 0 | 1 | 2 | 3 |
| - Annual energy savings (MWh) | 0 | 162 | 5092 | 5,254 |

**Objective**

By December 31, 2019, Hydro will have implemented additional measures to manage costs and further advanced customer service and energy efficiency initiatives for customers.

| INDICATORS | 2019 ACCOMPLISHMENTS |
|---|---|
| Completed priority capital investments for 2019 and identified 2020 capital projects. | As noted, in 2019 Hydro completed capital investments of $126.6 million to renew electricity generation and transmission assets. (A description of these expenditures is outlined in Issue 1.) While actual expenditures were lower than budget, Hydro evaluated criticality and risk to complete priority projects. |

| **ISSUE 2: ELECTRICITY RATES AND CUSTOMER SERVICE** | |
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| | In 2019, Hydro also prepared and submitted the 2020 Capital Budget Application (CBA) for regulatory approval. The 2020 CBA projects include the refurbishment of generation facilities, capital inspection of gas turbine generation equipment, and modernization and upgrade of terminal stations. |
| Identified and implemented measures to manage costs. | Hydro evaluated and implemented a number of innovation, productivity and cost management initiatives in 2019. These initiatives included: increased efficiencies to allow internal staff to complete work previously completed by contractors, overhauling rather than replacing more equipment based on economic analysis, investments in technologies, replacement of manual processes with online services, reductions in fleet and purchased services and optimization of revenue opportunities. Together, the initiatives resulted in approximately $5 million of sustainable annual cost savings.<br><br>*Operating Costs*<br>In 2019, cost management efforts and the capitalization of work previously budgeted as maintenance resulted in operating and maintenance costs of $133.1 million versus a budget of $136 million.<br><br>*Capital Costs*<br>As noted, in the 2020 Capital Budget Application filed with the PUB, Hydro realigned project scope and timing to better balance capital investments with customer expectations for cost management and reliability. The review of 2020 capital budget resulted in the reduction of planned capital expenditures of over $20 million. |
| Supported PUB process to examine options to mitigate rate impacts of Muskrat Falls, the Rate Mitigation Steering Committee, and advanced Hydro initiatives to contribute to rate mitigation. | In 2019,Hydro provided input to the PUB's review of options to reduce the impacts of the Muskrat Falls Project costs on electricity rates (the Reference) and with Nalcor presented evidence in the fall of 2019. The final report of the PUB was released in February 2020.<br><br>During the year, Hydro also worked with the Government of Newfoundland and Labrador, to advance initiatives to reduce expenses and increase revenue in support of rate mitigation. These initiatives include adding value to the energy surplus available from the Muskrat Falls Project and Holyrood performance credits awarded for greenhouse gas reductions. |

| **ISSUE 2: ELECTRICITY RATES AND CUSTOMER SERVICE** | |
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| Measured commercial customer satisfaction. | Hydro measures commercial customer satisfaction every two years. The findings from the survey are used to identify areas where Hydro is meeting customers' expectations and to identify areas for improvement.<br><br>The 2019 commercial customers' satisfaction survey found that 83 per cent are either very satisfied or somewhat satisfied. This result is slightly below the 85 per cent measured in 2017. |
| Completed priority customer service activities for Newfoundland Power and key accounts. | All priority customer service activities outlined in the 2019 account management plans were completed as planned.<br><br>Hydro developed annual account management plans for Newfoundland Power and other key accounts. These plans included scheduled customer meetings to discuss operations, reliability, projects, outage planning, account management, short/long term electricity system development, and energy efficiency. Also included was the communication of capital budget applications, specifically assigned assets charges, electricity rate changes, and general electricity system events that may impact these customers. |
| Delivered energy conservation programs to residential, commercial and industrial customers. | In 2019, Hydro continued to deliver energy efficiency programs to residential and commercial customers. These programs included the joint utility program offerings for residential and commercial customers through the takeCHARGE program delivered in partnership with Newfoundland Power, as well as Hydro's energy efficiency programs in isolated communities.<br><br>*takeCHARGE program*<br>In 2019 Hydro's residential and commercial program offerings achieved 2,266 MWh in annual savings.<br><br>*Residential Efficiency Program*<br>Hydro's residential portfolio includes five programs; insulation, thermostats, heat recovery ventilators ("HRV"), instant rebates, and the Residential Benchmarking Program. Together these programs helped residential customers save 794 MWh of energy in 2019.<br><br>*Isolated Systems Community Energy Efficiency Program*<br>In 2019, Hydro continued delivery of the Isolated Systems Community Energy Efficiency Program. This program promotes energy efficiency to residential and commercial customers in |

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|---|---|
| | communities served by diesel electricity systems in Labrador and on the island. During 2019, 1,160 residential and business customers in isolated communities benefited from the direct, free installation of energy efficient technologies to save 1,197 MWh of electricity.<br><br>*Business Efficiency Program*<br>Hydro also delivered programs to business customers in the company's interconnected and isolated areas in 2019. These programs provided facility audits and technical support to identify economical energy efficiency opportunities, and provide financial support for capital upgrades. In 2019, 13 facility audits were completed resulting in 234 MWh of annual energy savings.<br><br>*Industrial Customers*<br>In 2019, two industrial customers completed projects with anticipated annual energy savings of 5,092 MWh. Hydro provided financial support to these customers through the Industrial Energy Efficiency Program.<br><br>*Government Sponsored Programs*<br>Hydro was also involved in the delivery of government sponsored energy efficiency programs in 2019.<br>▪ Heat Pump Rebate Program: This government funded program, launched in October 2019, is managed by Hydro. As of December 31, 2019 Hydro received 953 heat pump rebate applications; 717 of these have been processed, resulting in 578 approvals or pre-approvals for the $1,000 rebate.<br>▪ Oil Heat Rebates: Hydro delivered an Energy Efficiency in Oil Heated Homes Program to its oil-heated customers on behalf of government. This program offers rebates for electronic and programmable thermostats, and insulation to oil-heated customers on a full cost recovery basis. The program launched in March 2019 and is funded through the Provincial portion of the Federal Low Carbon Economy Leadership Fund. For 2019 Hydro approved 1 insulation application under this program.<br>▪ Financing: In 2019 Hydro continued to work with the Provincial Government to deliver the 3-year Energy Efficient Loan Program. The program began in 2017 and offers a |

| ISSUE 2: ELECTRICITY RATES AND CUSTOMER SERVICE | |
|---|---|
| | reduced interest rate for insulation and heat pumps to accompany the utilities financing program. One application for financing was approved in 2019. |
| Complete planned energy efficiency initiatives for Hydro facilities and equipment. | In 2019, Hydro completed planned initiatives to enhance energy efficiency for Hydro facilities and equipment. The projects completed during the year, resulted in a savings of 239 MWh – significantly better than the target of 124 MWh savings.<br><br>More efficient lighting was installed at six diesel plants (McCallum, Cartwright, Charlottetown, Francois, Norman Bay, Makkovik), and at Cat Arm, Bay d'Espoir, Upper Salmon, and Paradise River plants. Heating improvements were also completed at the Cat Arm plant and a radiator replacement was started at Grey River diesel plant. |

## ISSUE 3: SAFETY

Achieving excellence in safety is Hydro's number one priority and safety is a shared core value. For Hydro, safety excellence is more than a way of operating - it is an integral part of Hydro's identity and strategy for the planning period and into the future. Hydro's pursuit of safety excellence encompasses the safety of employees, customers and the general public.

In 2019, many areas of Hydro sustained excellent safety performance. Hydro remains relentless in working to achieve a mature safety culture with employees identifying and addressing unsafe conditions and behaviours and accepting personal responsibility for their safety and the safety of others.

Achieving and maintaining excellent safety performance in all areas of the company remains an ongoing effort. In 2019, the number of safety incidents increased from 2018 with slips and trips and vehicle incidents continuing to comprise a significant portion of the total. To identify opportunities for improvement, Hydro completed investigations of these safety incidents and analyzed performance to identify areas for improving the design and delivery of its safety programs.

During 2019, Hydro continued employee training related to procedures for performing high-risk work including work protection code training, confined space training, and working at heights. Training courses related to completing safety investigations and safety coaching are also offered on an ongoing basis. To complement training, Hydro also works with Nalcor to deliver an employee injury prevention communication campaign with themes such as slips, trips and falls and driving safety. Occupational health and wellness assessments including hearing conservation and respiratory protection are also offered to Hydro employees. In 2018 and 2019, Hydro also introduced *The Working Mind* training as part of the Nalcor-wide Mental Health Strategy.

Starting in 2018, Hydro also began developing the processes and training to safely complete work on energized distribution lines. Live line work enables Hydro to complete required maintenance without a customer outage.

Customer safety, particularly around electricity outages, and public safety around electrical equipment and dams are also key elements of Hydro's safety commitment. During 2019, power outage safety and winter preparedness along with safety around hydroelectric dams and other electrical equipment continued to be key themes for Hydro's customer and public communications.

In 2019, Hydro also participated in an audit of the contractor safety management program used by Nalcor and Hydro to prevent injuries and illnesses due to the activities of contractors. Key findings are being actioned including improving documentation by implementing a contractor documentation management service.

<table>
<tr><th colspan="2">ISSUE 3: SAFETY</th></tr>
<tr><td colspan="2">Goal 1<br>By December 31, 2019, Hydro will have continued progress towards sustained safety excellence.</td></tr>
<tr><th>INDICATORS</th><th>2017-2019 ACCOMPLISHMENTS</th></tr>
<tr><td>Delivered electrical safety training for employees.</td><td>During the 2017-2019 planning period, Hydro continued to deliver safety training to employees. A summary of the activity for the period is presented below.
<table>
<tr><th>Training Program</th><th>2017</th><th>2018</th><th>2019</th><th>Total</th></tr>
<tr><td>Work Protection Code</td><td>264</td><td>276</td><td>211</td><td>751</td></tr>
<tr><td>Confined Space</td><td>42</td><td>57</td><td>97</td><td>196</td></tr>
<tr><td>Working at Heights</td><td>97</td><td>100</td><td>156</td><td>353</td></tr>
<tr><td>High Voltage Switching</td><td>22</td><td>47</td><td>8</td><td>77</td></tr>
<tr><td>Safety Reporting</td><td>46</td><td>58</td><td>56</td><td>150</td></tr>
<tr><td>Safety Coaching</td><td>35</td><td>28</td><td>59</td><td>122</td></tr>
<tr><td>Incident Investigation</td><td>10</td><td>41</td><td>24</td><td>75</td></tr>
<tr><td>The Working Mind</td><td>63</td><td>43</td><td>315</td><td>421</td></tr>
</table></td></tr>
<tr><td>Completed safety-related communications activities for</td><td>Safety-related communications for employees, customers and the general public continued over the planning period. Areas</td></tr>
</table>

| **ISSUE 3: SAFETY** | |
|---|---|
| employees and the general public. | of focus for these audiences reflected risks for each group.<br><br>*Employee Safety Communications*<br>During the planning period, Hydro delivered ongoing employee safety communications as part of Nalcor's company-wide campaign. Specific themes for each year reflected top trending injuries and internal communications included safety moments, fact sheets, posters, infographics and other education and awareness materials. Key topics for each year are noted below:<br>▪ 2017 topics: Vehicle safety; slips, trips and falls; mental health; alcohol and drug program; dropped objects; and, hand related injuries.<br>▪ 2018 topics: Vehicle safety; slips, trips and falls; hand related injuries; and mental health. In addition, with the legalization of cannabis in Canada, new education and awareness materials relating to cannabis in the workplace were developed.<br>▪ 2019 topics: Vehicle safety and mental health.<br><br>Some topics repeat for a number of years reflecting the need for multi-year campaigns to communicate and reinforce key safety messages.<br><br>*Public Safety Communications*<br>During the planning period, Hydro completed public and customer communication activities related to a variety of safety topics. Key activities for each year included:<br><br>2017<br>▪ Power line hazards: The power line safety communications and advertising campaign was delivered in partnership with Newfoundland Power, the Newfoundland and Labrador Construction Safety Association, and Workplace NL. This campaign promotes power line safety to the general public as well as targeted audiences such as heavy equipment operators and contractors.<br>▪ Public safety around hydroelectric facilities: Hydro promoted public safety around dams, dykes and hydroelectric facilities, including through social media and stakeholder engagements.<br>▪ Power outage safety: Hydro promoted power outage safety |

| **ISSUE 3: SAFETY** | |
|---|---|
| | with a particular emphasis during the winter months. This included digital content shared via its Twitter and Facebook channels.<br>▪ Safety around construction: With significant construction activity on new transmission lines in 2017, Hydro communicated about the about the associated dangers to the public and to our workers. Communication was issued through social media, radio and other channels regarding the risks of travelling on access roads and rights-of-way where workers and equipment could be present.<br>2018<br>Activities included planning, developing and implementing various public communications, with a focus on creating and distributing digital content on these safety topics. Hydro's Twitter and Facebook channels were used regularly to share safety information and promote greater awareness amongst the public. For example:<br>▪ Harsh weather events: Hydro circulated timely informational content promoting preparedness and safety, for example, what to do near downed power lines, and how to stay safe during, and prepare for, power outages.<br>▪ Public safety around hydroelectric facilities: In advance of long weekends, such as Victoria Day, Labour Day, Hydro promoted tips for staying safe around dams and hydroelectric facilities while fishing/ boating; and developed and published new educational information on the dangers of low-head dams.<br>▪ National Health and Safety Week: Hydro publicly circulated a series of posts with safety-oriented messages.<br>▪ Bishop's Falls dam: Hydro also promoted public safety at the Bishop's Falls dam site highlighting new safety features.<br>2019<br>Hydro continued customer and public safety communication activities related to power line safety, safety around hydroelectric dams and reservoirs, and power outage safety. Hydro also developed new informational material aimed at small contractors, promoting working safely around power lines and poles. |
| **Objective**<br>By December 31, 2019, Hydro will have continued progress towards sustained safety excellence by advancing safety programs. | |

| **ISSUE 3: SAFETY** | |
|---|---|
| INDICATORS | 2019 ACCOMPLISHMENTS |
| Delivered safety training for employees. | During 2019, Hydro delivered safety training for employees taking on new roles and refresher training for other employees. This training included technical training (e.g. work protection code refresher training for individuals working around electrical equipment), training required to meet legislative requirements (e.g. confined space entry) as well as safety coaching and safety incident investigation training.<br><br>*Work protection code, confined space entry, and working at heights training*<br>During 2019, required training for new Hydro employees, employees taking on new roles and responsibilities and employees needing refresher training was completed. In total, 211 employees completed work protection code training, 97 employees completed confined space entry training, and 156 employees completed working at heights training.<br><br>*High voltage principles and practices training*<br>During 2019, eight Hydro employees completed high voltage switching principles and practices training to refresh knowledge related to this high risk work activity in electricity operations.<br><br>*Safety coaching training*<br>Safety coaching training helps build the skills required to take action relating to at-risk behaviours by outlining a consistent approach to safety interactions and providing an opportunity to practice the approach. The majority of Hydro employees have completed safety coaching training but the training is offered periodically to new employees and others who have not completed the training. During 2019, 59 Hydro employees completed the training.<br><br>*Safe workplace observation program (SWOP) and incident investigation training*<br>SWOP and incident investigation training is offered annually to new employees and employees taking on new roles. In 2019, this training was completed as planned with 56 Hydro employees participating in SWOP training and 24 completing incident investigation training. |

| **ISSUE 3: SAFETY** | |
|---|---|
| | *The Working Mind*<br>The Working Mind-Managers/Supervisors is offered to supervisors and managers as part of Hydro's Mental Health Strategy. In 2019, 315 Hydro employees participated in The Working Mind training. |
| Completed employee safety communication activities. | During 2019, Hydro continued its employee safety communications (as part of Nalcor's employee safety communications campaign) and completed all planned activities. To support the organization's top trending injuries, communication efforts focused on key topics throughout the year, including vehicle safety and mental health. |
| Completed public safety communication activities related to power line safety, safety around electricity facilities, and power outage safety. | In 2019, Hydro completed customer and public safety communication activities related to power line safety, safety around hydroelectric dams and reservoirs, and power outage safety.<br><br>Activities included planning, developing and implementing various public communications, with a focus on creating and distributing digital content on these safety topics. Hydro's Twitter and Facebook channels were used regularly to share safety information and promote greater awareness amongst the public. For example:<br>▪ Around harsh weather events, Hydro circulated timely informational content promoting preparedness and safety, e.g. how to stay safe and prepare for power outages and keeping away from downed power lines.<br>▪ In advance of long weekends, Hydro promoted tips for staying safe around dams and hydroelectric facilities while fishing/ boating.<br>▪ Snowmobiling safety campaigns including staying clear of power lines, stations, and hydroelectric reservoirs.<br><br>Hydro also developed new informational material aimed at small contractors promoting working safely around power lines and poles. |

## 5. Opportunities and Challenges

During the 2020-2022 planning period, Hydro will build on accomplishments of the past and address future challenges and opportunities. The key challenges and opportunities that will be addressed reflect the next phase of Hydro's strategy execution.

Affordable Electricity Rates

A key driver of future electricity rates is the cost of the Muskrat Falls Project. Nalcor Energy's June 23, 2017 Muskrat Falls project update stated that average island residential electricity rates are expected to increase to 22.89 cents (¢) (plus HST) per kilowatt hour (kWh) in 2021 as a result of the project. During 2020-2022 planning period, Hydro will participate with Nalcor and the Government of Newfoundland and Labrador to evaluate and implement measures to mitigate the impact of Muskrat Falls on electricity rates and will monitor the outcomes of the PUB reference process. Hydro will also work to fulfill it's commitments to enhance efficiency and effectiveness in its operations and investments.

Reliability and Supply Adequacy

In keeping with its mandate, Hydro ensures there is a reliable electricity supply available to meet current customer needs and future growth. Core to this is maintaining Hydro's systems in reliable operating condition through a combination of planned maintenance, rehabilitation of existing assets, and replacement of assets that have reached the end of their useful lives. In the 2020-2022 planning period and beyond Hydro will sustain its focus on the completion of required maintenance and the identification and completion of required capital projects. Hydro will continue to consult with customers for their input and will strive to strike a balance between cost and reliability when making the significant decisions required during the planning period. Hydro will also ensure new assets are in service and reliable before taking permanent decisions on the future of the Holyrood Thermal Generating Station and other key assets in the electricity system.

Safety, Health and Environment

Achieving and maintaining excellent safety, health and environmental performance is an ongoing challenge. During the next planning period and beyond, Hydro will implement initiatives to safely complete high-risk work, complete electrical safety training to maintain employee competence, and continue employee injury prevention communications. In addition, Hydro will implement mental health initiatives and provide employees with access to tools and services to support health and wellness.

Customer safety and public safety around electrical equipment are also key elements of Hydro's safety commitment. Over the planning period, power line safety, power outage safety and winter preparedness along with safety around hydroelectric dams and other electrical equipment are key themes for Hydro's safety communications to customer and the public

Hydro will also focus on managing risk and minimizing the impact of operations on the environment. Over the planning period, Hydro's ISO 14001:2015 registered Environmental Management System will be used to support Hydro's focus on continuous improvement. As well, Hydro will continue to promote conservation and demand management by residential, commercial and industrial customers. Hydro will also support Government of Newfoundland and Labrador environmental initiatives related to electric vehicle infrastructure, electrification opportunities, and the integration of renewables in communities that rely on diesel for electricity generation.

# Appendix 1
# Provincial Electricity Generation and Transmission System

# Provincial Generation and Transmission Grid

**LEGEND**

- 735 kV
- 315 kV
- 230 kV
- 138 kV
- 69 kV
- LOW VOLTAGE
- 138kV CUSTOMER OWNED
- 69kV CUSTOMER OWNED
- HYDRO PLANT
- THERMAL PLANT
- TERMINAL STATION
- TERMINAL STATION & CONVERTER STATION
- FREQ. CONVERTOR
- NF. POWER
- CORNER BROOK PULP AND PAPER
- ALGONQUIN POWER
- MUSHUAU 1st NATION
- WIND GENERATION
- OPERATED BY NALCOR
- GAS TURBINE
- DIESEL PLANT

**DC LEGEND**

- ± 350 /± 200kV HVdc
- SUBMARINE CABLE
- ELECTRODE LINE
- ELECTRODE STATION

TO MUSKRAT FALLS

Labrador

Quebec

Newfoundland

Gulf of St. Lawrence

Atlantic Ocean

NOVA SCOTIA

L3501 L3502

L2001 L2002

L7053 L7052 L7051

RED BAY L' ANSE-AU-LOUP L' ANSE-AU-CLAIR L'ANSE AU DIABLE FORTEAU POINT SHOAL COVE CBL1,2&3 EDDIE'S COVE E. COOK'S HR. L'ANSE AUX MEADOWS ST. LUNAIRE ST. ANTHONY GOOSE COVE TL256 TL257B TL261 BEAR COVE ST. ANTHONY AIRPORT TL244 PLUM PT. MAIN BROOK TL257A CROQUE NEW FEROLLE CONCHE RODDICKTON RODDICKTON MINI-HYDRO ENGLEE TL241 EDDIE'S COVE W. PORT AU CHOIX HAWKES BAY RIVER OF PONDS TL221 BELLBURNS PETER'S BARREN DANIELS HR. TL262 PORTLAND CREEK TL227 TL259 PARSONS POND JACKSON'S ARM CAT ARM FLEUR DE LYS PACQUET TL260 LA SCIE SEAL COVE CONEY ARM COW HEAD RATTLE BROOK TL253 VENAM'S BIGHT SNOOK'S ARM BOTTOM WATERS TL227 JACKSON'S ARM TAP WEST-PORT SALLY'S COVE BERRY HILL NORRIS PT. TL252 HAMPDEN NP SPRINGDALE TRITON ROCKY HR. WOODY PT. TAYLOR'S POND TL239 HAMPDEN TAP TL223 INDIAN RIVER ROBERT'S ARM GLENBURNIE TL229 TL247 TL251 TL224 SOUTH BROOK TROUT RIVER WILTONDALE TL226 TL225 DEER LAKE TL222 BISHOP'S FALLS BOTWOOD LEWISPORTE GANDER BAY WESLEYVILLE CORNER BROOK HOWLEY TL245 TL243 GRAND FALLS COBBS POND FRENCHMAN'S COVE NP HINDS LAKE TL248 TL210 GANDER NP ST. BRENDAN'S CoGENERATION BUCHANS TL205 TL235 GLEN-WOOD MASSEY DRIVE TL228 TL232 SANDY BROOK STONY BROOK TL211 R-FIELD TAP GAMBO STEPHENVILLE DUCK POND BONAVISTA BOTTOM BROOK TL209 TL233 TL280 TL264 TL231 TL204 INDIAN HEAD NP STAR LAKE L3501 L3502 N.S. DAM & SPILLWAY TL263 MILTON NP LOOKOUT BROOK TL214 TL269 TL250 CLARENVILLE OLD PERLICAN NEW CHELSEA UPPER SALMON TL270 GRANITE CANAL TL234 BAY D'ESPOIR TL206 TL202 CARBONEAR DOYLES L2001 L2002 TL215 GRANDY BK. ST. ALBAN'S ENGLISH HR. WEST TL267 SUNNYSIDE TL207 TL203 TL237 TL220 TL219 TL212 CONNE RIVER PARADISE RIVER OXEN POND TL218 TL268 TL265 TL236 HARDWOODS GRAND BAY LONG LAKE NP LAPOILE BURGEO McCALLUM BARACHOIX COME BY CHANCE WESTERN AVALON HOLY-ROOD TL266 DOWDEN'S POINT CAPE RAY PORT AUX BASQUES RAMEA GREY RIVER FRANCOIS GAULTOIS RENCONTRE EAST MONKSTOWN TL208 TL201 TL242 PASS IS. SEAL COVE BELLEORAM VOISEY BAY NICKEL TL217 SOLDIERS POND HERMITAGE HR. BRETON PETIT FORTE SOUTH EAST BIGHT CLARKE'S POND CAPE BROYLE GARNISH LINTON LAKE MARYSTOWN SALT POND GRAND BANK NP FERMEUSE LAWN FALL POND ST. LAWRENCE TREPASSEY

POINT ACONI WOODBINE BIG LORRAINE

Quebec: NAIN NATUASHISH HOPEDALE POSTVILLE MAKKOVIK MENIHEK RIGOLET CHURCHILL FALLS TWIN FALLS L1301 LABRADOR CITY L2304 L2303 WABUSH GOOSE BAY NORTH WEST RIVER CARTWRIGHT BLACK TICKLE TS3 TS1 MUD LAKE PARADISE RIVER NORMAN BAY L3101 L3102 L1302 CHARLOTTETOWN TS2 MUSKRAT FALLS L3501 L3502 PORT HS ST. LEWIS MARY'S HR. L'ANSE-AU-LOUP

Labrador: CHANGE ISLANDS TWILLINGATE FOGO ISLAND FAREWELL HEAD TL254 BOYD'S COVE

0 50 100 KILOMETRES

Revised: January 30, 2020

**Appendix 2**

**Newfoundland and Labrador Hydro Consolidated Financial Statements**

# NEWFOUNDLAND AND LABRADOR HYDRO
# CONSOLIDATED FINANCIAL STATEMENTS
# December 31, 2019

Deloitte LLP
5 Springdale Street
Suite 1000
St. John's, NL  A1E 0E4
Canada

Tel: 709-576-8480
Fax: 709-576-8460
www.deloitte.ca

# Independent Auditor's Report

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

**Opinion**
We have audited the consolidated financial statements of Newfoundland and Labrador Hydro (the "Company"), which comprise the consolidated statement of financial position as at December 31, 2019, and the consolidated statements of profit and comprehensive income, 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, 2019, 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.

**Emphasis of Matter – Restated Comparative Information**
We draw attention to Note 29 to the financial statements, which explains that certain comparative information presented for December 31, 2018 has been restated. Our opinion is not modified in respect to this matter.

**Responsibilities of Management and Those Charged with Governance for the Financial Statements**
Management is responsible for the preparation and fair presentation of the financial statements in accordance with 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.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

Deloitte LLP

Chartered Professional Accountants
February 28, 2020

**NEWFOUNDLAND AND LABRADOR HYDRO**
**CONSOLIDATED STATEMENT OF FINANCIAL POSITION**

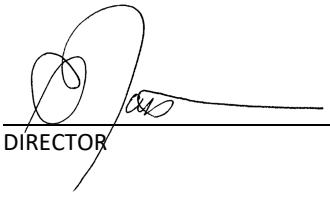
| *As at December 31 (millions of Canadian dollars)* | Notes | **2019** | 2018 |
|---|---|---|---|
| **ASSETS** | | | |
| Current assets | | | |
| Cash | | **66** | 30 |
| Short-term investments | | **-** | 34 |
| Trade and other receivables | 5 | **146** | 149 |
| Inventories | 6 | **114** | 107 |
| Prepayments | | **8** | 7 |
| Deferred asset | 7 | **9** | 21 |
| Total current assets | | **343** | 348 |
| Non-current assets | | | |
| Property, plant and equipment | 8 | **2,731** | 2,652 |
| Intangible assets | 9 | **5** | 6 |
| Right-of-use assets | 10 | **2** | - |
| Investment in joint arrangement | | **1** | 1 |
| Other long-term assets | 11 | **199** | 176 |
| Total assets | | **3,281** | 3,183 |
| Regulatory deferrals | 12 | **123** | 159 |
| Total assets and regulatory deferrals | | **3,404** | 3,342 |
| **LIABILITIES AND EQUITY** | | | |
| Current liabilities | | | |
| Short-term borrowings | 14 | **233** | 189 |
| Trade and other payables | 13 | **168** | 140 |
| Current portion of long-term debt | 14 | **7** | 7 |
| Deferred credits | | **1** | - |
| Current portion of deferred contributions | 15 | **2** | 2 |
| Derivative liability | 23 | **9** | 21 |
| Total current liabilities | | **420** | 359 |
| Non-current liabilities | | | |
| Long-term debt | 14 | **1,776** | 1,784 |
| Deferred contributions | 15 | **25** | 24 |
| Decommissioning liabilities | 16 | **15** | 15 |
| Lease liabilities | 17 | **2** | - |
| Employee future benefits | 18 | **123** | 105 |
| Total liabilities | | **2,361** | 2,287 |
| Shareholder's equity | | | |
| Share capital | 19 | **23** | 23 |
| Contributed capital | 19 | **152** | 152 |
| Reserves | | **(22)** | (13) |
| Retained earnings | | **877** | 822 |
| Total equity | | **1,030** | 984 |
| Total liabilities and equity | | **3,391** | 3,271 |
| Regulatory deferrals | 12 | **13** | 71 |
| Total liabilities, equity and regulatory deferrals | | **3,404** | 3,342 |

Commitments and contingencies (Note 25) and Subsequent event (Note 30)

*See accompanying notes*

On behalf of the Board:

DIRECTOR



DIRECTOR

**NEWFOUNDLAND AND LABRADOR HYDRO**
**CONSOLIDATED STATEMENT OF PROFIT AND COMPREHENSIVE INCOME**

| *For the year ended December 31 (millions of Canadian dollars)* | Notes | **2019** | 2018 (Restated - Note 29) |
|---|---|---|---|
| Energy sales | | **720** | 660 |
| Other revenue | | **28** | 31 |
| Revenue | | **748** | 691 |
| Fuels | | **217** | 189 |
| Power purchased | | **99** | 84 |
| Operating costs | 20 | **184** | 178 |
| Transmission rental | | **22** | 21 |
| Depreciation and amortization | 8,9 | **103** | 105 |
| Net finance expense | 21 | **89** | 85 |
| Other expense | 22 | **8** | 14 |
| Expenses | | **722** | 676 |
| Profit before regulatory adjustments | | **26** | 15 |
| Regulatory adjustments | 12 | **(37)** | (47) |
| Profit for the year | | **63** | 62 |
| Other comprehensive income | | | |
| Total items that may or have been reclassified to profit or loss | | | |
| Actuarial (loss) gain on employee future benefits | 18 | **(9)** | 9 |
| Other comprehensive (loss) income for the year | | **(9)** | 9 |
| Total comprehensive income for the year | | **54** | 71 |

*See accompanying notes*

**NEWFOUNDLAND AND LABRADOR HYDRO**
**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**

| *(millions of Canadian dollars)* | Notes | Share Capital | Contributed Capital | Employee Benefit Reserve | Retained Earnings | Total |
|---|---|---|---|---|---|---|
| **Balance at January 1, 2019** | | **23** | **152** | **(13)** | **822** | **984** |
| **Profit for the year** | | **-** | **-** | **-** | **63** | **63** |
| **Other comprehensive loss** | | **-** | **-** | **(9)** | **-** | **(9)** |
| **Total comprehensive (loss) income for the year** | | **-** | **-** | **(9)** | **63** | **54** |
| **Contributed capital** | **19** | **-** | **1** | **-** | **-** | **1** |
| **Regulatory adjustment** | **19** | **-** | **(1)** | **-** | **-** | **(1)** |
| **Dividends** | **19** | **-** | **-** | **-** | **(8)** | **(8)** |
| **Balance at December 31, 2019** | | **23** | **152** | **(22)** | **877** | **1,030** |
| | | | | | | |
| Balance at January 1, 2018 | | 23 | 150 | (22) | 768 | 919 |
| Profit for the year | | - | - | - | 62 | 62 |
| Other comprehensive income | | - | - | 9 | - | 9 |
| Total comprehensive income for the period | | - | - | 9 | 62 | 71 |
| Contributed capital | 19 | - | 3 | - | - | 3 |
| Regulatory adjustment | 19 | - | (1) | - | - | (1) |
| Dividends | 19 | - | - | - | (8) | (8) |
| Balance at December 31, 2018 | | 23 | 152 | (13) | 822 | 984 |

*See accompanying notes*

**NEWFOUNDLAND AND LABRADOR HYDRO**
**CONSOLIDATED STATEMENT OF CASH FLOWS**

| *For the year ended December 31 (millions of Canadian dollars)* | Notes | **2019** | 2018 |
|---|---|---|---|
| Operating activities | | | |
| Profit for the year | | **63** | 62 |
| Adjustments to reconcile profit to cash provided from operating activities: | | | |
| Depreciation and amortization | 8,9 | **103** | 105 |
| Regulatory adjustments | 12 | **(37)** | (47) |
| Finance income | 21 | **(14)** | (13) |
| Finance expense | 21 | **103** | 98 |
| Other | | **16** | 11 |
| | | **234** | 216 |
| Changes in non-cash working capital balances | 27 | **31** | (25) |
| Interest received | | **1** | 2 |
| Interest paid | | **(104)** | (104) |
| Net cash provided from operating activities | | **162** | 89 |
| Investing activities | | | |
| Additions to property, plant and equipment | | **(170)** | (197) |
| Additions to intangible assets | | **-** | (1) |
| Contributions to sinking funds | 11 | **(7)** | (7) |
| Decrease in long-term investment | | **-** | 34 |
| Decrease (increase) in short-term investment | | **34** | (19) |
| Increase in reserve fund | 11 | **(13)** | (12) |
| Changes in non-cash working capital balances | 27 | **(6)** | (23) |
| Net cash used in investing activities | | **(162)** | (225) |
| Financing activities | | | |
| Proceeds from long-term debt | | **-** | 316 |
| Dividends paid | 19 | **(8)** | (8) |
| Increase (decrease) in short-term borrowings | 14 | **44** | (180) |
| Increase in contributed capital | | **-** | 1 |
| Other | | **-** | 2 |
| Rate stabilization plan refund | | **-** | (3) |
| Net cash provided from financing activities | | **36** | 128 |
| Net increase (decrease) in cash | | **36** | (8) |
| Cash, beginning of the year | | **30** | 38 |
| Cash, end of the year | | **66** | 30 |

*See accompanying notes*

## 1. DESCRIPTION OF BUSINESS

Newfoundland and Labrador Hydro (Hydro or the Company) is incorporated under a special act of the Legislature of the Province of Newfoundland and Labrador (the Province). The principal activity of Hydro is the generation, transmission and sale of electricity. Hydro's operations include both regulated and non-regulated activities. Hydro is a 100% owned subsidiary of Nalcor Energy (Nalcor). Hydro's head office is located at 500 Columbus Drive in St. John's, Newfoundland and Labrador, A1B 0C9, Canada.

Hydro holds interests in the following entities:

A 65.8% interest in Churchill Falls (Labrador) Corporation Limited (Churchill Falls). Churchill Falls is incorporated under the laws of Canada and owns and operates a hydroelectric generating plant and related transmission facilities situated in Labrador which has a rated capacity of 5,428 megawatts (MW).

A 51% interest in Lower Churchill Development Corporation (LCDC), an inactive subsidiary. LCDC is incorporated under the laws of Newfoundland and Labrador and was established with the objective of developing all or part of the hydroelectric potential of the Lower Churchill River.

## 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). Hydro has adopted accounting policies which are based on the IFRS applicable as at December 31, 2019, and includes individual IFRS, International Accounting Standards (IAS), and interpretations made by the IFRS Interpretations Committee and the Standing Interpretations Committee.

These annual audited consolidated financial statements have been prepared on a historical cost basis, except for financial instruments at fair value through profit or loss (FVTPL) 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 Hydro's Board of Directors (the Board) on February 28, 2020.

### 2.2 Basis of Consolidation

The annual audited consolidated financial statements include the financial statements of Hydro, its subsidiary companies, its proportionate share of investments in joint arrangements and its share of investments over which Hydro exercises significant influence using the equity method of accounting. In addition, the financial statements of all structured entities, for which Hydro has been determined the primary beneficiary, are included in these annual audited consolidated financial statements. Intercompany transactions and balances have been eliminated upon consolidation.

### 2.3 Cash and Cash Equivalents and Short-Term Investments

Cash and cash equivalents consist of amounts on deposit with a Schedule 1 Canadian Chartered bank, 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.

### 2.4 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.

**2.5 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 Hydro's 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, Hydro recognizes such parts as individual assets with specific useful lives and depreciation. Likewise, when a major inspection is performed, its cost is recognized in the carrying amount of the plant and equipment as a replacement if the recognition criteria are satisfied. All other repairs and maintenance costs are recognized in profit or loss as incurred.

Depreciation commences when the assets are ready for their intended use. Residual values, useful lives and method of depreciation are reviewed at the end of each year and adjusted prospectively, if appropriate. As per Board Order P.U. 30 (2019), Hydro was approved to recover gains and losses through accumulated amortization and to record removal costs through depreciation. To comply with IAS 16, the adjustments related to the recovery of gains and losses through accumulated amortization and removal depreciation are presented as a regulatory adjustment in Note 12. The depreciation rates used are as follows:

| | |
|---|---|
| Generation plant | |
| Hydroelectric | 25 to 110 years |
| Thermal | 20 to 70 years |
| Diesel | 3 to 70 years |
| Transmission | |
| Lines | 26 to 65 years |
| Terminal stations | 20 to 60 years |
| Distribution system | 20 to 60 years |
| Other assets | 5 to 70 years |

Hydroelectric generation plant includes the powerhouse, turbines, governors and generators, as well as water conveying and control structures, including dams, dikes, tailraces, penstocks 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 station assets are used to step up voltages of electricity for transmission 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.

Churchill Falls

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

| | |
|---|---|
| Hydroelectric generation plant | 20 to 100 years |
| Transmission and terminals | 20 to 65 years |
| Service facilities and other | 5 to 50 years |

**2.6 Intangible Assets**

Intangible assets that are expected to generate future economic benefit and are measurable, including computer software costs, costs of technical services and studies 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:

| | |
|---|---|
| Feasibility studies | 22 years |
| Computer software | 7 years |

**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 Consolidated Statement of Profit and Comprehensive Income 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, Hydro 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. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted. Value in use is generally computed by reference to the present value of future cash flows expected to be derived from non-financial assets.

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

**2.9 Investment in Joint Arrangement**

A joint arrangement is an arrangement in which two or more parties have joint control. Control exists when Hydro 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.

Hydro accounts for its investment in Churchill Falls by recognizing its share of assets, liabilities and profit or loss in relation to its interest in the 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 Income reflects the share of the profit or loss of the joint venture.

**2.10 Employee Future Benefits**

(i) Pension Plan

Employees participate in the Province's Public Service Pension Plan (Plan), a multi-employer defined benefit plan. Contributions by Hydro 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

Hydro provides group life insurance and health care benefits on a cost-shared basis to retired employees, in addition to a severance payment upon retirement.

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 Hydro'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 Board Order No. P.U. 36 (2015), Hydro recognizes the amortization of employee future benefit actuarial gains and losses in the Consolidated Statement of Profit and Comprehensive 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.

**2.11 Provisions**

A provision is a liability of uncertain timing or amount. A provision is recognized if Hydro 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.

**2.12 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 Income if the liability is short-term in nature.

**2.13 Revenue from Contracts with Customers**

Hydro recognizes revenue from contracts with customers related to the sale of electricity to Regulated industrial, utility and rural customers in Newfoundland and Labrador and to Non-Regulated industrial, utility and external market customers.

Revenue is measured based on the consideration specified in a contract with a customer and excludes amounts collected on behalf of third parties. Hydro recognizes revenue when it transfers control of a product or service to a customer.

Revenue from the sale of energy is recognized when Hydro satisfies its performance obligation by transferring energy to the customer. 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 other certain major industrial customers are either at rates under the terms of the applicable contracts, or at market rates. Hydro recognizes revenue at the amount to which it has the right to invoice, which corresponds directly to the value of Hydro's performance to date.

Churchill Falls 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 year until 2041.

**2.14 Leasing**

Lessee Accounting

Hydro assesses whether a contract is or contains a lease, at inception of a contract. Hydro 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, Hydro 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, Hydro uses its incremental borrowing rate.

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

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

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

**2.15 Foreign Currencies**

Transactions in currencies other than Hydro's functional currency (foreign currencies) are recognized using the exchange rate in effect at the date of transaction, approximated by the prior month end close rate. At the end of each reporting period, monetary items denominated in foreign currencies are translated at the rates of exchange in effect at the period end date. Foreign exchange gains and losses not included in regulatory deferrals are recorded in the Consolidated Statement of Profit and Comprehensive Income as other expense.

**2.16 Income Taxes**

Hydro is exempt from paying income taxes under Section 149(1) (d.2) of the Income Tax Act.

**2.17 Financial Instruments**

Classification and Initial Measurement

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

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

Financial Assets at Amortized Cost

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

Hydro's financial assets at amortized cost include cash, short-term investments, trade and other receivables and sinking fund investments.

Financial Assets at FVTOCI

Financial assets measured at FVTOCI are those that have contractual cash flows arising on specific dates, consisting solely of principal and interest, and that are held within a business model whose objective is to collect the contractual cash flows and to sell the financial asset. Any changes in the carrying amount of these assets other than foreign exchange gains and losses, impairment gains and losses, and interest income are recognized in other comprehensive income accumulated in the fair value reserve. When these assets are derecognized, the cumulative gains or losses previously recognized in other comprehensive income are reclassified to profit or loss.

Hydro's financial assets measured at FVTOCI include reserve fund investments.

Financial assets at FVTPL

Financial assets that do not meet the criteria for being measured at amortized cost or FVTOCI are measured at FVTPL. Financial assets at FVTPL are measured at fair value at the end of each reporting period, with any fair value gains or losses recognized in profit or loss to the extent they are not part of a designated hedging relationship.

Hydro's financial assets measured at FVTPL include derivative instruments not part of a designated hedging relationship.

Financial Liabilities at Amortized Cost

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

Hydro's financial liabilities at amortized cost include trade and other payables, short-term borrowings and long-term debt.

Derivative Instruments

Derivative instruments are utilized by Hydro to manage risk. Hydro'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 designed and effective as a hedging relationship.

Derecognition of Financial Instruments

Hydro 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.

Hydro 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

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

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

For all other financial instruments, Hydro 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, Hydro 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.

**2.18 Government Grants**

Government grants are recognized when there is reasonable assurance that Hydro 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 Hydro recognizes as expenses the related costs for which the grants are intended to compensate. Specifically, government grants whose primary condition is that Hydro 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 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 Hydro with no future related costs are recognized in the Consolidated Statement of Profit and Comprehensive Income in the period in which they become receivable.

**2.19 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. Hydro's allowed rate of return on rate base based upon Board Order No. P.U. 30 (2019) is 5.4% in 2019 and 5.5% in 2018. Hydro applies various regulator approved 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.

### 3.1 Use of Judgments

(i) Property, Plant and Equipment

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

(ii) 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.

(iii) Determination of CGUs

Hydro's accounting policy relating to impairment of non-financial assets is described in Note 2.8. In applying this policy, Hydro groups assets into the smallest identifiable group 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.

(iv) Discount Rates

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

(v) 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.

(vi) Leases

Definition of a lease

At inception of a contract, Hydro 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, Hydro assesses whether the contract involves the use of an identified asset, Hydro has the right to obtain substantially all of the economic benefits from use of the asset throughout the period of use and Hydro has the right to direct the use of the asset.

Lease extension and termination options

In determining the lease term, Hydro 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 Hydro's assets. The useful lives of property, plant and equipment are determined by independent specialists and reviewed annually by Hydro. 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.

Pursuant to Board Order No. P.U. 30 (2019), the PUB approved a change in estimated service lives of Hydro's property, plant and equipment. The impact of this change for the year ended December 31, 2019 would be impracticable to calculate given the volume of assets and resources required to calculate depreciation using two sets of service lives.

In addition, the PUB approved a depreciation methodology change where asset removal costs will be included in depreciation rates and gains and loss on retirement will be recovered through accumulated depreciation. To comply with IAS 16, removal depreciation, the deferral of removal costs incurred and the deferral of gains and losses on retirement will be presented as regulatory adjustments. Please refer to the Notes 12(j) and 12(q).

(ii) Decommissioning Liabilities

Hydro 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 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.

(iii) Employee Future Benefits

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

(iv) Revenue

In the absence of a signed agreement with Hydro-Québec relating to the AEB, Churchill Falls has an agreement with Hydro-Québec to continue to use the 2008 AEB on an interim basis until September 1, 2019. Now that a final judgment has been received in the Declaratory Judgment Case, the Parties are in the process of negotiating the value of the final AEB that will establish the Continuous Energy for the term of the Renewed Power Contract.

(v) Leases incremental borrowing rate

Hydro 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.

### 3.3 Use of Assumptions

Deferred Assets and Derivative Liabilities

Effective October 1, 2015, Hydro entered into a power purchase agreement (PPA) with Nalcor Energy Marketing Corporation (Nalcor Energy Marketing) which allows for the purchase of available recapture energy from Hydro for resale by Nalcor Energy Marketing in export markets or through agreements with counterparties. Additionally, the PPA allows for the use of Hydro's transmission service rights by Nalcor Energy Marketing to deliver electricity, through rights which are provided to Hydro pursuant to a Transmission Service Agreement with Hydro-Québec dated April 1, 2009. In September 2016, the terms of the PPA were amended to require a 60 day termination notice by either party. This replaced the previous termination clause of 90 days prior to the end of the operating year. Management's assumption is that the term of the PPA at December 31, 2019, will continue for at least the next 5 months.

Fair values relating to Hydro's financial instruments and derivatives that have been classified as Level 3 have been determined using inputs for the assets or liabilities that are not readily observable. Certain of these fair values are classified as Level 3 as the transactions do not occur in an active market, or the terms extend beyond the period for which a quoted price is available.

Hydro's PPA with Nalcor Energy Marketing is accounted for as a derivative instrument, where Hydro determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability, nor based on a valuation technique that uses only data from observable markets. These derivative transactions are initially measured at fair value and the expected difference is deferred. Subsequently, the deferred difference is recognized in other comprehensive income (loss) on an appropriate basis over the life of the related derivative instrument but not later than when the valuation is wholly supported by observable market data or the transaction has occurred.

Hydro has elected to defer the difference between the fair value of the power purchase derivative liability upon initial recognition and the transaction price of the power purchase derivative liability and to amortize the deferred asset on a straight-line basis over its effective term (Note 7). These methods, when compared with alternatives, were determined by Management to most accurately reflect the nature and substance of the transactions.

## 4. CURRENT AND FUTURE CHANGES IN ACCOUNTING POLICIES

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

- IFRS 16 – Leases[1]
- IFRS 9 – Prepayment Features with Negative Compensation[1]
- IAS 19 – Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)[1]
- IAS 28 – Long-term Interests in Associates and Joint Ventures (Amendments to IAS 28)[1]
- IAS 23 – Borrowing Costs (Amendments to IAS 23)[1]
- IFRS 11 – Joint Arrangements (Amendments to IFRS 11 )[1]
- IAS 1 – Presentation of Financial Statements[2] and IAS 8 – Accounting Policies, Changes in Accounting Estimates and Errors[2] (Amendments to IAS 1 and IAS 8)

[1] Effective for annual periods beginning on or after January 1, 2019.
[2] Effective for annual periods beginning on or after January 1, 2020.

### 4.1 IFRS 16 – Leases

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

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

Impact of the new definition of a lease

Hydro has not elected to apply the practical expedient available on transition to IFRS 16, not to reassess whether a contract is or contains a lease at the date of initial application. In preparation for the first-time application of IFRS 16, Hydro has carried out an implementation project which has shown that the new definition in IFRS 16 will not significantly change the scope of contracts that meet the definition of a lease for Hydro.

Impact on Lessee Accounting

Former operating leases

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

Applying IFRS 16, for all leases (except as noted below), Hydro:

a) recognizes right-of-use assets and lease liabilities in the Consolidated Statement of Financial Position, initially measured at the present value of future lease payments;
b) recognizes depreciation of right-of-use assets and interest on lease liabilities in the Consolidated Statement of Profit and Comprehensive Income; and
c) separates the total amount of cash paid into a principal portion (presented within financing activities) and interest (presented within operating activities) in the Consolidated Statement of Cash Flows.

For short-term leases (lease term of 12 months or less) and leases of low-value assets (such as personal computers and office furniture), Hydro has opted to recognize a lease expense on a straight-line basis as permitted by IFRS 16. This expense is presented within operating costs in the Consolidated Statement of Profit and Comprehensive Income.

Former finance leases

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

Impact on Lessor Accounting

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

Financial impact of the application of IFRS 16

On transition to IFRS 16, Hydro recognized lease liabilities in relation to leases which had previously been classified as operating leases under IAS 17. These liabilities were measured at the present value of the remaining lease payments, discounted using Hydro's incremental borrowing rate as of January 1, 2019. The weighted average incremental borrowing rates applied to the lease liabilities on January 1, 2019 were 2.3 – 3.4%. The associated right-of-use assets were measured at the amount equal to the corresponding lease liabilities totalling $2.2 million.

| *(millions of Canadian dollars)* | |
|---|---|
| Operating lease commitments disclosed as at December 31, 2018 | - |
| Additional operating lease commitments recognized under IFRS 16 as at January 1, 2019 | 3 |
| Total operating lease commitments | 3 |
| Discounted using the incremental borrowing rates of 2.3 – 3.4% | 1 |
| Extension and termination options reasonably certain to be exercised | 1 |
| **Lease liability recognized on January 1, 2019** | **2** |

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

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

**4.2 IFRS 9 – Prepayment Features with Negative Compensation**

Under IFRS 9, a debt instrument can be measured at amortized cost or at FVTOCI, provided that the contractual cash flows are 'solely payments of principal and interest on the principal amount outstanding' (the SPPI criterion) and the instrument is held within the appropriate business model for that classification. The amendments to IFRS 9 clarify that a financial asset passes the SPPI criterion regardless of the event or circumstance that causes the early termination of the contract and irrespective of which party pays or receives reasonable compensation for the early termination of the contract. The application of these amendments to IFRS 9 did not have a material impact on Hydro's annual audited consolidated financial statements.

**4.3 IAS 19 – Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)**

The amendments to IAS 19 address the accounting when a plan amendment, curtailment or settlement occurs during a reporting period. The amendments also clarify that an entity first determines any past service cost, or a gain or loss on settlement, without considering the effect of the asset ceiling. This amount is recognized in profit or loss. An entity then determines the effect of the asset ceiling after the plan amendment, curtailment or settlement. Any change in that effect, excluding amounts included in the net interest, is recognized in other comprehensive income. The application of these amendments to IAS 19 did not have a material impact on Hydro's annual audited consolidated financial statements.

**4.4 IAS 28 – Long-term Interests in Associates and Joint Ventures (Amendments to IAS 28)**

The amendments clarify that an entity applies IFRS 9 to long-term interests in an associate or joint venture to which the equity method is not applied but that, in substance, form part of the net investment in the associate or joint venture (long-term interests). This clarification is relevant because it implies that the expected credit loss model in IFRS 9 applies to such long-term interests. The amendments also clarified that, in applying IFRS 9, an entity does not take account of any losses of the associate or joint venture, or any impairment losses on the net investment, recognized as adjustments to the net investment in the associate or joint venture that arise from applying IAS 28 Investments in Associates and Joint Ventures. The application of these amendments to IAS 28 did not have a material impact on Hydro's annual audited consolidated financial statements.

**4.5 IAS 23 – Borrowing Costs (Amendments to IAS 23)**

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

**4.6 IFRS 11 – Joint Arrangements (Amendments to IFRS 11)**

The amendment to IFRS 11 clarifies that when an entity obtains joint control of a business that is a joint operation, the entity does not remeasure previously held interests in that business.

The application of these amendments to IFRS 11 did not have a material impact on Hydro's annual audited consolidated financial statements.

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

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

## 5. TRADE AND OTHER RECEIVABLES

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Trade receivables | **118** | 121 |
| Due from related parties | **16** | 18 |
| Other receivables | **26** | 27 |
| Allowance for doubtful accounts | **(14)** | (17) |
| | **146** | 149 |

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| 0-60 days | **135** | 135 |
| 60+ days | **11** | 14 |
| | **146** | 149 |

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Allowance for doubtful accounts, beginning of the year | **(17)** | (17) |
| Change in balance during the year | **3** | - |
| Allowance for doubtful accounts, end of the year | **(14)** | (17) |

## 6. INVENTORIES

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Fuel | **65** | 57 |
| Materials | **46** | 47 |
| Other | **3** | 3 |
| | **114** | 107 |

Fuel inventory includes No. 6 fuel in the amount of $53.4 million (2018 - $47.6 million). The cost of inventories recognized as an expense during the year is $218.6 million (2018 - $192.0 million) and is included in operating costs and fuels.

## 7. DEFERRED ASSET

The deferred asset related to Hydro's power purchase agreement (PPA) with Nalcor Energy Marketing is amortized into income on a straight-line basis over the assumed 12 month term of the contract, which commenced on January 1, 2019. The components of change are as follows:

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Deferred asset, beginning of the year | **21** | 31 |
| Additions | **9** | 21 |
| Amortization | **(21)** | (31) |
| Deferred asset, end of the year | **9** | 21 |

## 8. PROPERTY, PLANT AND EQUIPMENT

| *(millions of Canadian dollars)* | Generation Plant | Transmission and Distribution | Other | Construction in Progress | Total |
|---|---|---|---|---|---|
| Cost | | | | | |
| Balance at January 1, 2018 | 1,838 | 1,191 | 260 | 66 | 3,355 |
| Additions | - | - | - | 202 | 202 |
| Disposals | (11) | (9) | (3) | - | (23) |
| Transfers | 90 | 107 | 21 | (219) | (1) |
| Other adjustments | (1) | - | - | 2 | 1 |
| Decommissioning liabilities and revisions | - | (1) | - | - | (1) |
| Balance at December 31, 2018 | 1,916 | 1,288 | 278 | 51 | 3,533 |
| **Additions** | **-** | **-** | **-** | **173** | **173** |
| **Disposals** | **(6)** | **(4)** | **(4)** | **-** | **(14)** |
| **Transfers** | **81** | **69** | **15** | **(165)** | **-** |
| **Other adjustments** | **1** | **-** | **-** | **-** | **1** |
| **Balance at December 31, 2019** | **1,992** | **1,353** | **289** | **59** | **3,693** |
| Depreciation | | | | | |
| Balance at January 1, 2018 | 509 | 186 | 95 | - | 790 |
| Depreciation | 54 | 34 | 15 | - | 103 |
| Disposals | (8) | (2) | (2) | - | (12) |
| Balance at December 31, 2018 | 555 | 218 | 108 | - | 881 |
| **Depreciation** | **59** | **30** | **12** | **-** | **101** |
| **Disposals** | **(2)** | **(1)** | **(3)** | **-** | **(6)** |
| **Other adjustments** [1] | **(6)** | **(6)** | **(2)** | **-** | **(14)** |
| **Balance at December 31, 2019** | **606** | **241** | **115** | **-** | **962** |
| Carrying value | | | | | |
| Balance at January 1, 2018 | 1,329 | 1,005 | 165 | 66 | 2,565 |
| Balance at December 31, 2018 | 1,361 | 1,070 | 170 | 51 | 2,652 |
| **Balance at December 31, 2019** | **1,386** | **1,112** | **174** | **59** | **2,731** |

[1] In Board Order P.U. 48 (2018), the PUB approved a 2018 cost deferral of $18.5 million related to the differential in the 2018 depreciation expense associated with the proposed change in depreciation methodology. Pursuant to Board Order No. P.U. 30 (2019), the PUB approved Hydro's proposed depreciation methodology and the reclassification of $13.6 million of the 2018 cost deferral to property, plant and equipment as referenced in Note 12(a).

## 9. INTANGIBLE ASSETS

| *(millions of Canadian dollars)* | Computer Software | Feasibility Studies | Assets Under Development | Total |
|---|---|---|---|---|
| Cost | | | | |
| Balance at January 1, 2018 | 13 | 2 | - | 15 |
| Additions | - | - | 1 | 1 |
| Transfers | 1 | - | (1) | - |
| Balance at December 31, 2018 | 14 | 2 | - | 16 |
| **Transfers** | **1** | **-** | **-** | **1** |
| **Balance at December 31, 2019** | **15** | **2** | **-** | **17** |
| Amortization | | | | |
| Balance at January 1, 2018 | 7 | 1 | - | 8 |
| Amortization | 2 | - | - | 2 |
| Balance at December 31, 2018 | 9 | 1 | - | 10 |
| **Amortization** | **2** | **-** | **-** | **2** |
| **Balance at December 31, 2019** | **11** | **1** | **-** | **12** |
| Carrying value | | | | |
| Balance at January 1, 2018 | 6 | 1 | - | 7 |
| Balance at December 31, 2018 | 5 | 1 | - | 6 |
| **Balance at December 31, 2019** | **4** | **1** | **-** | **5** |

## 10. RIGHT-OF-USE ASSETS

Hydro leases various properties and has several contracts for easements. Contracts are typically entered into for a fixed period of 2 to 100 years. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The lease agreements do not impose any covenants, but leased assets may not be used as security for borrowing purposes.

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

| *(millions of Canadian dollars)* | Property |
|---|---|
| Cost | |
| Balance at January 1, 2019 | 2 |
| **Additions** | - |
| **Balance at December 31, 2019** | **2** |
| Depreciation | |
| Balance at January 1, 2019 | - |
| **Depreciation** | - |
| **Balance at December 31, 2019** | **-** |
| Carrying value | |
| Balance at January 1, 2019 | 2 |
| **Balance at December 31, 2019** | **2** |

## 11. OTHER LONG-TERM ASSETS

| *As at December 31 (millions of Canadian dollars)* | | **2019** | 2018 |
|---|---|---|---|
| Reserve fund | (a) | **25** | 12 |
| Sinking funds | (b) | **174** | 164 |
| | | **199** | 176 |

(a) In 2007, Churchill Falls commenced the creation of a $75.0 million segregated reserve fund pursuant to the terms of the Shareholder's Agreement to contribute towards the funding of capital expenditures related to Churchill Falls' existing facilities and their replacement. In December 2019, $18.8 million (2018 - $18.8 million) was invested into the fund as part of the Shareholder's Agreement to re-establish the $75.0 million withdrawn in recent years. Hydro has recorded its 65.8% proportionate share of the amount invested of $12.3 million (2018 - $12.4 million).

This fund must remain in place until the end of the Shareholder's 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.

Hydro's proportionate share of the reserve fund consists of the following:

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Reserve fund, beginning of the year | **12** | - |
| Principal contributions | **13** | 12 |
| Reserve fund, end of the year | **25** | 12 |
| Less: current portion | **-** | - |
| | **25** | 12 |

Hydro's proportionate share of reserve fund contributions due for the next five years are as follows:

| *(millions of Canadian dollars)* | 2020 | 2021 | 2022 | 2023 | 2024 |
|---|---|---|---|---|---|
| Reserve fund contributions | 12 | 6 | 6 | - | - |

(b) As at December 31, 2019, sinking funds include $174.0 million (2018 - $164.4 million) related to repayment of Hydro's long-term debt. Sinking fund investments consist of bonds, debentures and coupons issued by, or guaranteed by, the Government of Canada, provincial governments or Schedule 1 banks, and have maturity dates ranging from 2022 to 2033.

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 2.51% to 6.82% (2018 – 2.57% to 6.82%).

The sinking funds consist of the following:

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Sinking funds, beginning of the year | **164** | 156 |
| Contributions | **7** | 7 |
| Change in sinking fund investments in own debentures | **(8)** | (10) |
| Earnings | **11** | 11 |
| Sinking funds, end of the year | **174** | 164 |

Sinking fund instalments due over the next five years are as follows:

| *(millions of Canadian dollars)* | 2020 | 2021 | 2022 | 2023 | 2024 |
|---|---|---|---|---|---|
| Sinking fund instalments | 7 | 7 | 7 | 7 | 7 |

## 12. REGULATORY DEFERRALS

| *(millions of Canadian dollars)* | | January 1 2019 | Reclass & Disposition | Regulatory Activity | **December 31 2019** | Remaining Recovery Settlement Period (years) |
|---|---|---|---|---|---|---|
| Regulatory asset deferrals | | | | | | |
| 2018 cost deferral | (a) | 19 | (19) | - | **-** | n/a |
| 2018 revenue deficiency | (b) | - | (2) | 1 | **(1)** | 0.2 |
| 2019 revenue deficiency | (c) | - | (53) | 52 | **(1)** | 1.4 |
| Deferred energy conservation costs | (d) | 9 | - | - | **9** | n/a |
| Deferred lease costs | (e) | 2 | - | (1) | **1** | 1.4 |
| Energy supply deferral | (f) | 77 | (69) | 27 | **35** | n/a |
| Foreign exchange losses | (g) | 50 | - | (2) | **48** | 22.0 |
| Business system transformation program | (h) | - | - | 3 | **3** | n/a |
| Rate stabilization plan (RSP) | (i) | - | 16 | - | **16** | n/a |
| Retirement asset pool | (j) | - | 9 | 2 | **11** | n/a |
| Other | (k,l,m,n,x) | 2 | - | - | **2** | n/a |
| | | 159 | (118) | 82 | **123** | |
| Regulatory liability deferrals | | | | | | |
| Insurance amortization and proceeds | (o) | (3) | - | - | **(3)** | n/a |
| Rate stabilization plan (RSP) | (i) | (67) | 108 | (41) | **-** | n/a |
| Firm energy purchase | (p) | - | - | (2) | **(2)** | n/a |
| Removal provision | (q) | - | (4) | (4) | **(8)** | n/a |
| Other | (r,s,t,u) | (1) | - | 1 | **-** | n/a |
| | | (71) | 104 | (46) | **(13)** | |

### 12.1 Regulatory Adjustments Recorded in the Consolidated Statement of Profit and Comprehensive Income

| *For the year ended December 31 (millions of Canadian dollars)* | | **2019** | 2018 |
|---|---|---|---|
| RSP amortization | | **4** | (10) |
| RSP fuel deferral | | **34** | 2 |
| RSP interest | | **2** | 4 |
| Rural rate adjustment | | **1** | - |
| Total RSP activity | (i) | **41** | (4) |
| 2018 cost deferral | (a) | **-** | (19) |
| 2018 revenue deficiency | (b) | **(1)** | - |
| 2019 revenue deficiency | (c) | **(52)** | - |
| Amortization of deferred foreign exchange losses | (g) | **2** | 2 |
| Deferred lease costs | (e) | **1** | 1 |
| Energy supply deferral | (f) | **(27)** | (25) |
| Firm energy purchase | (p) | **2** | - |
| Non-customer contributions in aid of construction | (v) | **(1)** | (1) |
| Removal provision | (q) | **4** | - |
| Retirement asset pool | (j) | **(2)** | - |
| Business system transformation program | (h) | **(3)** | - |
| Other | (k,l,m,n,o,r,s,t,u,w,x) | **(1)** | (1) |
| | | **(37)** | (47) |

The following section describes Hydro's regulatory assets and liabilities 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 year and profit for 2019 would have decreased by $36.7 million (2018 – $46.6 million).

**12.(a) 2018 Cost Deferral**

In Board Order No. P.U. 48 (2018), the Board approved the 2018 cost deferral of $18.5 million related to the differential in the 2018 depreciation, loss on retirement and removal costs associated with the proposed change in depreciation methodology. As per Board Order No. P.U. 30 (2019), the Board approved the reclassification of the 2018 cost deferral to an increase to property, plant and equipment of $13.6 million, the creation of a $9.4 million asset retirement pool, a $3.8 million removal pool liability and an increase to deferred contributions of $0.7 million.

**12.(b) 2018 Revenue Deficiency**

In Board Order P.U. 30 (2019), the Board approved the 2018 Revenue Deficiency of $0.8 million. The Revenue Deficiency consists of $2.3 million which was approved to be recovered through a transfer to the RSP and a refund to customers of $1.5 million. A refund of $0.6 million was paid to industrial customers in October 2019 with the remaining balance of $0.9 million due to be refunded to the Labrador Rural Interconnected customers in February 2020.

**12.(c) 2019 Revenue Deficiency**

In Board Order P.U. 30 (2019), the Board approved the 2019 Revenue Deficiency of $51.8 million. The Revenue Deficiency consists of $52.6 million which was approved to be recovered through a transfer to the RSP, $0.1 million to be recovered over a 20 month period and a refund to customers of $0.9 million. A refund of $0.3 million was paid to Industrial customers in October 2019 which resulted in a December 31, 2019 balance in the 2019 Revenue Deficiency of $0.6 million. The remaining refund of $0.6 million to the Labrador Rural Interconnected customers is scheduled to be paid in February 2020.

**12.(d) Deferred Energy Conservation Costs**

In 2019, Hydro deferred $1.5 million (2018 - $1.5 million) in Energy Conservation Costs associated with an electrical conservation demand management program for residential, industrial, and commercial sectors. As per Board Order No. P.U. 22 (2017), Hydro recovered $1.4 million (2018 – $1.2 million) of the balance through a rate rider.

**12.(e) Deferred Lease Costs**

In Board Order No's. P.U. 17 (2016), P.U. 23 (2016) and No. P.U. 49 (2016) the Board approved amortization of lease costs associated with mobile diesel units at HTGS over a period of five years. In 2019, Hydro recorded amortization of $1.3 million (2018 - $1.3 million) of the deferred lease costs.

**12.(f) Energy Supply Deferrals**

Pursuant to Board Order No. P.U. 22 (2017), the Board approved the deferral of Energy Supply costs using three specific deferral accounts: the Energy Supply, Holyrood Conversion and Isolated Systems Supply cost deferrals. In 2019, Hydro recorded a net increase to the deferrals of $29.6 million (2018 - $25.3 million) with recovery determined through an annual application process. In Board Order No. P.U. 21 (2019), the Board approved the recovery of the 2018 supply cost deferral of $22.0 million from the balance of the RSP. Board Order No. P.U. 30 (2019) approved the recovery of the 2015-2017 supply deferrals of $65.4 million through a transfer of $47.0 million to the RSP with the remaining balance to be recovered over a 20 month period commencing in October 2019. During 2019 Hydro recovered $2.7 million from customers.

**12.(g) 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 2019, amortization expense of $2.2 million (2018 - $2.2 million) was recorded.

**12.(h) Business System Transformation Program**

As per Board Order No.'s P.U. 23 (2019) and P.U. 30 (2019), the Board approved the deferral of business system transformation program costs commencing in 2018. The recovery of the deferral is subject to a future Board order. During the year, Hydro deferred $2.5 million relating to both 2018 and 2019.

**12.(i) 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, load and associated interest. 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.

During 2019, Hydro recorded a net decrease in the RSP balance of $89.9 million (2018 - decrease of $7.2 million) resulting in a balance from customers of $16.2 million (2018 - $67.0 million liability). The decrease in the RSP liability is due to adjustments related to the GRA and the 2018 energy supply deferrals. Pursuant to Board Order No. P.U. 30 (2019), the Board ordered the recovery of $52.6 million associated with the 2019 Revenue Deficiency and $2.3 million associated with the 2018 Revenue Deficiency from the RSP. As per Board Order No.'s P.U. 21 (2019) and P.U. 30 (2019), the Board approved the recovery of a portion of the 2015-2017 supply deferrals of $47.0 million and the 2018 supply cost deferral of $22.0 million from the RSP. The normal operation of the RSP resulted in a net deferral of $40.7 million (2018 – $3.8 million).

**12.(j) Retirement Asset Pool**

As per Board Order No. P.U. 30 (2019), the Board approved Hydro's proposed depreciation methodology which includes the deferral of gains and losses on retirement of assets. The deferral will be recovered through future depreciation expense. The depreciation methodology and corresponding retirement asset pool was approved effective January 1, 2018. In addition, the Board approved the reclassification of the 2018 cost deferral which results in a transfer of a $9.4 million deferred asset to the retirement asset pool. Hydro also deferred $1.7 million of 2019 retirement asset activity resulting in a total balance of $11.1 million.

**12.(k) Deferred Foreign Exchange on Fuel**

Hydro purchases fuel for Holyrood Thermal Generating Station (HTGS) in USD. The RSP allows Hydro to defer variances in fuel prices (including foreign exchange fluctuations). During 2019, Hydro recognized in regulatory assets, foreign exchange gains on fuel purchases of $1.0 million (2018 - $1.1 million loss).

**12.(l) Phase Two Hearing Costs**

Pursuant to Board Order No. P.U. 13 (2016), Hydro received approval to defer consulting fees and salary related costs 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 net increase to regulatory assets of $0.2 million (2018 - $0.1 million) for a total deferred balance of $1.4 million (2018 - $1.2 million).

**12.(m) Hearing Costs**

As per Board Order No. P.U. 30 (2019), the Board approved the deferral of $1.7 million in hearing costs relating to the 2017 General Rate Application hearing and the Cost of Service hearing to be amortized over a three year period commencing 2018. In 2019, Hydro recorded amortization for 2018 and 2019 of $1.1 million resulting in a net balance of $0.6 million.

**12.(n) Asset Disposal**

As per Board Order No. P.U. 49 (2016), the Board 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.

**12.(o) 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 amortization in regulatory liabilities. During 2019, Hydro recorded a decrease to regulatory liabilities resulting from amortization of $0.6 million (2018 - $0.6 million) related to the assets.

**12.(p) Firm Energy Purchase**

Pursuant to Board Order No. P.U. 3 (2020), the Board approved the deferral of savings associated with firm energy power purchases. Hydro recorded a regulatory liability of $1.4 million in 2019 (2018 - $nil). The refund of the balance is to be determined in a future Board Order.

**12.(q) Removal Provision**

As per Board Order No. P.U. 30 (2019), the Board approved Hydro's proposed depreciation methodology which includes the provision for removal costs. The depreciation methodology and corresponding removal provision was approved effective January 1, 2018. In addition, the Board approved the reclassification of the 2018 cost deferral which results in a transfer of a regulatory liability of $3.8 million to the removal pool. Hydro also recorded a net increase to the provision relating to 2019 activity of $4.1 million resulting in a total balance of $7.9 million.

**12.(r) Hydraulic Resources Optimization Deferral Account**

In Board Order P.U. 49 (2018), a deferral account to capture the revenues and costs associated with the hydraulic optimization activities was approved. For the year ended December 31, 2019, the balance of hydraulic optimization activities is a net gain of $0.3 million (2018 - $nil) recorded as a deferred liability.

**12.(s) Deferred Specifically Assigned Industrial Revenue**

In Board Order No. P.U. 7 (2018), Hydro was ordered to establish a deferral account, commencing April 1, 2018, to track the difference between the approved specifically assigned charges used to derive interim rates and the amount that would be charged if the proposed methodology in the general rate application was approved. During 2019, this balance was eliminated as part of the 2018 Revenue Deficiency approved in Board Order P.U. 30 (2019).

**12.(t) 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 from 2014 to 2017. The Board 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 2019, Hydro recorded amortization expense of $0.2 million (2018 – $0.2 million).

**12.(u) 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 $0.3 million (2018 - $0.3 million) are deferred as a regulatory liability.

**12.(v) Non-Customer Contributions in Aid of Construction**

Pursuant to Board Order No. P.U. 1 (2017), Hydro recognized amortization of deferred contributions in aid of construction (CIAC) from entities which are not customers in profit or loss. During 2019, Hydro recorded $0.7 million (2018 - $1.0 million) non-customer CIAC amortization as a regulatory adjustment. In the absence of rate regulation, IFRS requires non-customer CIACs to be recorded as contributed capital with no corresponding amortization. As a result, during 2019 Hydro also recorded an increase of $0.7 million (2018 - $1.0 million) to contributed capital to recognize the amount that was reclassified to profit or loss.

**12.(w) 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 2019, Hydro recorded $nil (2018 - $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 income. As a result, during 2019 Hydro also recorded a decrease of $nil (2018 - $0.2 million) to other comprehensive income to recognize the amount that was reclassified to profit or loss.

**12.(x) Reliability and Resource Adequacy Study**

Pursuant to Board Order No. P.U. 29 (2019), the Board approved the deferral of costs associated with the Reliability and Resource Adequacy proceeding. Hydro deferred $0.2 million in 2019 (2018 - $nil). The recovery of the balance is to be determined in a future Board Order.

## 13. TRADE AND OTHER PAYABLES

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Trade payables | **102** | 75 |
| Accrued interest payable | **25** | 25 |
| Due to related parties | **7** | 7 |
| Other payables | **34** | 33 |
| | **168** | 140 |

## 14. DEBT

### 14.1 Short-term Borrowings

On August 9, 2019, Hydro signed an extension to its $200.0 million CAD or USD equivalent committed revolving term credit facility resulting in a new maturity date of July 27, 2021. As at December 31, 2019, there were no amounts drawn on the facility (2018 - $nil). Borrowings in CAD may take the form of Prime Rate Advances, Bankers' Acceptances (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, London Interbank Offer Rate (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 $300.0 million government guaranteed promissory note program to fulfill its short-term funding requirements. As at December 31, 2019, there were $233.0 million in promissory notes outstanding with a maturity date of January 7, 2020 bearing an average interest rate of 1.82% (2018 - $189.0 million bearing an interest rate of 1.77%). Upon maturity, the promissory note was reissued.

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 Bankers' Acceptance (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, 2019 (2018 - $nil).

Churchill Falls has issued three irrevocable letters of credit totalling $2.0 million (2018 - $2.0 million), $1.0 million of which does not impact the borrowing limit of the operating credit facility (2018 - $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 Municipal Affairs and Environment.

### 14.2 Long-term Debt

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

| *As at December 31 (millions of Canadian dollars)* | Face Value | Coupon Rate % | Year of Issue | Year of Maturity | **December 31 2019** | December 31 2018 |
|---|---|---|---|---|---|---|
| Hydro | | | | | | |
| Y* | 300 | 8.40 | 1996 | 2026 | **296** | 296 |
| AB* | 300 | 6.65 | 2001 | 2031 | **305** | 305 |
| AD* | 125 | 5.70 | 2003 | 2033 | **124** | 124 |
| AF | 500 | 3.60 | 2014/2017 | 2045 | **481** | 480 |
| 1A | 600 | 3.70 | 2017/2018 | 2048 | **640** | 641 |
| Total | 1,825 | | | | **1,846** | 1,846 |
| Less: Sinking fund investments in own debentures | | | | | **63** | 55 |
| | | | | | **1,783** | 1,791 |
| Less: Sinking fund payments due within one year | | | | | **7** | 7 |
| Total | | | | | **1,776** | 1,784 |

*Sinking funds have been established for these issues.
**Hydro's V Series debentures had a balance of $0.2 million outstanding as at December 31, 2019.

Hydro’s promissory notes and debentures are unsecured and unconditionally guaranteed as to principal and interest and, where applicable, sinking fund payments, by the Province, with exception of Series 1A which is borrowed directly from the Province. 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, 2019 was $8.6 million (2018 - $6.9 million).

## 15. DEFERRED CONTRIBUTIONS

Hydro has received contributions in aid of construction of property, plant and equipment. These contributions are deferred and amortized to other revenue over the life of the related property, plant and equipment asset.

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Deferred contributions, beginning of the year | **26** | 24 |
| Additions | **1** | 2 |
| Other adjustments | **1** | 2 |
| Amortization | **(1)** | (2) |
| Deferred contributions, end of the year | **27** | 26 |
| Less: current portion | **(2)** | (2) |
| | **25** | 24 |

## 16. DECOMMISSIONING LIABILITIES

Hydro has recognized liabilities associated with the retirement of portions of the HTGS and the disposal of Polychlorinated Biphenyls (PCB).

The reconciliation of the beginning and ending carrying amounts of decommissioning liabilities for December 31, 2019 are as follows:

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Decommissioning liabilities, beginning of the year | **15** | 15 |
| Accretion | **-** | - |
| Decommissioning liabilities, end of the year | **15** | 15 |

The total estimated undiscounted cash flows required to settle the HTGS obligations at December 31, 2019 are $15.2 million (2018 - $15.2 million). Payments to settle the liability are expected to occur between 2020 and 2024. 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 2.0% (2018 - 2.3%). Hydro has recorded $14.1 million (2018 - $13.8 million) related to HTGS obligations.

The total estimated undiscounted cash flows required to settle the PCB obligations at December 31, 2019 are $1.3 million (2018 - $1.1 million). Payments to settle the liability are expected to occur between 2020 and 2025. 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 2.1% (2018 - 2.5%). Hydro has recorded $1.2 million (2018 - $0.9 million) related to PCB obligations.

Hydro'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 Hydro'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 Hydro is required to remove, a decommissioning liability for those assets will be recognized at that time.

## 17. LEASE LIABILITIES

| *(millions of Canadian dollars)* | 2019 |
|---|---|
| **Maturity analysis - contractual undiscounted cash flows** | |
| Less than one year | - |
| One to five years | - |
| More than five years | 7 |
| **Total undiscounted lease liabilities as at December 31, 2019** | **7** |
| | |
| **Lease liabilities included in the Consolidated Statement of Financial Position** | |
| Current lease liabilities | - |
| Non-current lease liabilities | 2 |
| **Total lease liabilities as at December 31, 2019** | **2** |

**AMOUNTS RECOGNIZED IN THE CONSOLIDATED STATEMENT OF PROFIT AND COMPREHENSIVE INCOME**

| *For the year ended December 31 (millions of Canadian dollars)* | | 2019 |
|---|---|---|
| Variable lease payments not included in the measurement of leases | (a) | **28** |

(a) Variable lease payments not included in the measurement of leases include payments made to Nalcor for power generated from assets which are owned by the Province. These variable lease payments are included in power purchased in the Consolidated Statement of Profit and Comprehensive Income.

The total cash outflow for leases amount to $28.2 million for the year ended December 31, 2019.

## 18. EMPLOYEE FUTURE BENEFITS

### 18.1 Pension Plan

Employees participate in the Province's Public Service Pension Plan, a multi-employer defined benefit plan. The employer's contributions for the year ended December 31, 2019 of $9.6 million (2018 - $9.6 million) are expensed as incurred.

### 18.2 Other Benefits

Hydro 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 upon retirement. In 2019, cash payments to beneficiaries for its unfunded other employee future benefits were $3.3 million (2018 - $3.0 million). An actuarial valuation was performed as at December 31, 2019.

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Accrued benefit obligation, beginning of the year | **105** | 109 |
| Current service cost | **5** | 5 |
| Past service cost | **3** | - |
| Interest cost | **4** | 4 |
| Benefits paid | **(3)** | (3) |
| Actuarial loss (gain) | **9** | (9) |
| Transfers and other | **-** | (1) |
| Accrued benefit obligation, end of the year | **123** | 105 |

When an employee transfers to a related party, the associated accrued benefit obligation is allocated to each respective party based on years of service.

| *For the year ended December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Component of benefit cost | | |
| Current service cost | **5** | 5 |
| Past service cost | **3** | - |
| Interest cost | **4** | 4 |
| Total benefit expense for the year | **12** | 9 |

The significant actuarial assumptions used in measuring the accrued benefit obligations and benefit expenses are as follows:

| | **2019** | 2018 |
|---|---|---|
| Discount rate - benefit cost | **3.90%** | 3.55% |
| Discount rate - accrued benefit obligation | **3.20%** | 3.90% |
| Rate of compensation increase | **3.50%** | 3.50% |

Assumed healthcare trend rates:

| | **2019** | 2018 |
|---|---|---|
| Initial health care expense trend rate | **5.85%** | 5.85% |
| Cost trend decline to | **3.60%** | 4.50% |

Current rate 5.85%, reducing linearly to 3.6% in 2040 and thereafter.

A 1% change in assumed health care trend rates would have had the following effects:

| *Increase (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Current service and interest cost | **2** | 2 |
| Accrued benefit obligation | **20** | 17 |

| *Decrease (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Current service and interest cost | **(1)** | (1) |
| Accrued benefit obligation | **(15)** | (13) |

## 19. SHAREHOLDER'S EQUITY

### 19.1 Share Capital

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Common shares of par value of $1 each | | |
| Authorized - 25,000,000 | | |
| Issued, paid and outstanding - 22,503,942 | **23** | 23 |

### 19.2 Contributed Capital

| *As at December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Contributed capital, beginning of the year | **152** | 150 |
| Additions | **1** | 3 |
| Amortization | **(1)** | (1) |
| Contributed capital, end of the year | **152** | 152 |

During 2019, the Churchill Falls (Labrador) Corporation Trust (the Trust) contributed capital in the amount of $nil (2018 - $1.3 million). In addition, Lower Churchill Management Corporation (LCMC) contributed $0.7 million (2018 - $1.7 million) in additions to property, plant and equipment. Pursuant to Board Order No. P.U. 1 (2017), Hydro recognized $0.7 million (2018 - $1.0 million) in amortization as a regulatory adjustment.

### 19.3 Dividends

| *For the year ended December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Declared during the year | | |
| Final dividend for prior year: $0.05 per share (2018 - $0.06) | **1** | 1 |
| Interim dividend for current year: $0.29 per share (2018 - $0.30) | **7** | 7 |
| | **8** | 8 |

## 20. OPERATING COSTS

| *For the year ended December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Salaries and benefits | **114** | 112 |
| Maintenance and materials | **31** | 32 |
| Professional services | **10** | 10 |
| Rental and royalty | **4** | 4 |
| Travel and transportation | **6** | 7 |
| Equipment rental | **2** | 2 |
| Insurance | **6** | 5 |
| Other operating costs | **11** | 6 |
| | **184** | 178 |

## 21. NET FINANCE EXPENSE

| *For the year ended December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Finance income | | |
| Interest on sinking fund | **11** | 11 |
| Other interest income | **3** | 2 |
| | **14** | 13 |
| Finance expense | | |
| Long-term debt | **92** | 90 |
| Debt guarantee fee | **9** | 7 |
| Other | **4** | 4 |
| | **105** | 101 |
| Interest capitalized during construction | **(2)** | (3) |
| | **103** | 98 |
| Net finance expense | **89** | 85 |

## 22. OTHER EXPENSE

| *For the year ended December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Loss on disposal of property, plant and equipment | **7** | 11 |
| Foreign exchange loss | **-** | 2 |
| Other | **1** | 1 |
| Other expense | **8** | 14 |

## 23. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

### 23.1 Fair Value

The estimated fair values of financial instruments as at December 31, 2019 and December 31, 2018 are based on relevant market prices and information available at the time. Fair value estimates are based on valuation techniques which are significantly affected by the assumptions used including the amount and timing of future cash flows and discount rates reflecting various degrees of risk. As such, the fair value estimates below are not necessarily indicative of the amounts that Hydro might receive or incur in actual market transactions.

As a significant number of Hydro'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 Hydro 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, Hydro 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 for the years ended December 31, 2019 and December 31, 2018.

| *As at (millions of Canadian dollars)* | Level | **Carrying Value** | **Fair Value** | Carrying Value | Fair Value |
|---|---|---|---|---|---|
| | | **December 31, 2019** | | December 31, 2018 | |
| Financial assets | | | | | |
| Sinking funds - investments in Hydro debt issue | **2** | **63** | **75** | 55 | 63 |
| Sinking funds - other investments | **2** | **174** | **211** | 164 | 195 |
| Reserve fund | **2** | **25** | **25** | 12 | 12 |
| Financial liabilities | | | | | |
| Derivative liability | **3** | **9** | **9** | 21 | 21 |
| Long-term debt (including amount due within one year before sinking funds) | **2** | **1,846** | **2,242** | 1,846 | 2,100 |

The fair value of cash and cash equivalents, 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 the derivative liability relating to the PPA with Nalcor Energy Marketing and represent the future value provided to Nalcor Energy Marketing through the contract.

The following table summarizes quantitative information about the valuation techniques and unobservable inputs used in the fair value measurement of Level 3 financial instruments as at December 31, 2019:

| *(millions of Canadian dollars)* | Carrying Value | Valuation Techniques | Significant Unobservable Input(s) | Range |
|---|---|---|---|---|
| Derivative liability (PPA) | 9 | Modelled pricing | Volumes (MWh) | 18-29% of available generation |

The derivative liability arising under the PPA is designated as a Level 3 instrument as certain forward market prices and related volumes are not readily determinable to estimate a portion of the fair value of the derivative liability. Hence, fair value measurement of this instrument is based upon a combination of internal and external pricing and volume estimates. As at December 31, 2019, the effect of using reasonable alternative assumptions for volume inputs to valuation techniques may have resulted in $nil to +$0.9 million change in the carrying value of the power purchase derivative liability.

### 23.2 Risk Management

Hydro is exposed to certain credit, liquidity and market price risks through its operating, investing and financing activities. Financial risk is managed in accordance with Hydro's Board approved Financial Risk Management 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 Hydro's expected future cash flows.

Credit Risk

Hydro's expected future cash flow is 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 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 minimal, as Hydro's cash deposits are held by a Schedule 1 Canadian Chartered Bank with a rating of A+ (Standard and Poor's).

Credit exposure on Hydro'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 funds portfolio:

| | **Issuer Credit Rating** | **Fair Value of Portfolio (%)** | **Issuer Credit Rating** | **Fair Value of Portfolio (%)** |
|---|---|---|---|---|
| | **2019** | | 2018 | |
| Provincial Governments | **AA- to AAA** | **17.30%** | AA- to AAA | - |
| Provincial Governments | **A- to A+** | **27.16%** | A- to A+ | 44.98% |
| Provincially owned utilities | **AA- to AAA** | **26.00%** | AA- to AAA | - |
| Provincially owned utilities | **A- to A+** | **29.54%** | A- to A+ | 55.02% |
| | | **100.00%** | | 100.00% |

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. Investment 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 Government of Canada, holdings of any one issuer are limited to 10% of the total principal amount of the portfolio. The following credit risk table provides information on credit exposure 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 (%)** |
|---|---|---|---|---|
| | **2019** | | 2018 | |
| Provincial Governments | **A- to A+** | **40.50%** | A- to A+ | 38.57% |
| Provincially owned utilities | **AA- to AAA-** | **8.93%** | AA- to AAA- | - |
| Provincially owned utilities | **A- to A+** | **4.54%** | A- to A+ | 8.91% |
| Schedule 1 Canadian banks | **AA- to AAA** | **12.17%** | AA- to AAA | 14.15% |
| Schedule 1 or 2 Canadian banks | **A- to A+** | **33.86%** | A- to A+ | 38.37% |
| | | **100.0%** | | 100.0% |

Credit exposure on derivative assets is limited by the Financial Risk Management Policy, which restricts available counterparties for hedge transactions to Schedule 1 Canadian Chartered Banks, and Federally Chartered US Banks.

Hydro's exposure to credit risk on its energy sales and associated accounts receivable is determined by the credit quality of its customers. Hydro's three largest customers account for 82.3% (2018 - 81.8%) of total energy sales and 63.4% (2018 – 62.4%) of accounts receivable. Energy sales for the three largest customers include $501.2 million (2018 - $455.9 million) for regulated Hydro, as well as $39.8 million (2018 - $33.1 million) for Non-Regulated Hydro. Churchill Falls' exposure to credit risk on energy sales is limited, as Churchill Falls' main customer, Hydro-Québec is an investment grade utility.

Liquidity Risk

Hydro 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 is mainly provided through cash and cash equivalents on hand, funds from operations, and a $300.0 million promissory note program. In addition, Hydro maintains a $200.0 million (2018 - $200.0 million) unsecured demand operating facility with its primary banker. Churchill Falls also maintains a $23.0 million (2018 - $22.5 million) minimum cash balance, business interruption insurance, as well as a $10.0 million (2018 - $10.0 million) unsecured credit facility with its banker.

Long-term liquidity risk for Hydro is managed by the issuance of a portfolio of debentures 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 the contractual maturities of Hydro's financial liabilities, including principal and interest, as at December 31, 2019:

| *(millions of Canadian dollars)* | <1 Year | 1-3 Years | 3-5 years | > 5 Years | Total |
|---|---|---|---|---|---|
| Trade and other payables | 168 | - | - | - | 168 |
| Short-term borrowings | 233 | - | - | - | 233 |
| Derivative liability | 9 | - | - | - | 9 |
| Long-term debt including sinking funds | 7 | 14 | 14 | 1,790 | 1,825 |
| Interest | 93 | 185 | 185 | 1,127 | 1,590 |
| | 510 | 199 | 199 | 2,917 | 3,825 |

Market Risk

In the course of carrying out its operating, financing and investing activities, Hydro 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 Hydro has significant exposure include those relating to prevailing interest rates, foreign exchange rates, most notably the USD/CAD, and current commodity prices, most notably the spot prices for fuel, electricity, and No. 6 fuel. These exposures are addressed as part of the Financial Risk Management Policy.

*Interest Rates*

Changes in prevailing interest rates will impact the fair value of financial assets and liabilities which includes Hydro's cash and cash equivalents, short-term investments and sinking funds. Expected future cash flows associated with those financial instruments can also be impacted. The impact of a 0.5% change in interest rates on net income and other comprehensive income associated with cash and cash equivalents and short-term debt was negligible throughout 2019 due to the short time period to maturity. There was no impact on profit and other comprehensive income associated with long-term debt as all of Hydro's long-term debt has fixed interest rates.

Changes in prevailing interest rates will impact the fair value of financial assets classified as FVTOCI, which includes Churchill Falls' reserve fund. Expected cash flows from these assets are also impacted in certain circumstances, such as when reserve fund securities are sold prior to maturity. The impact to other comprehensive income for a 0.5% decrease or increase in interest rate would be +$0.1 million and -$0.1 million, respectively.

*Foreign Currency and Commodity Exposure*
Hydro's primary exposure to both foreign exchange and commodity price risk arises from its purchases of No. 6 fuel for consumption at the HTGS, and these risks are mitigated through operation of the RSP.

As at December 31, 2019, trade and other payables included balances of $0.2 million (2018 - $0.3 million) denominated in USD.

The components of the change impacting the carrying value of the derivative asset and derivative liability for the years ended December 31, 2019 and December 31, 2018 are as follows:

| ***(millions of Canadian dollars)*** | **Level 3** |
|---|---|
| **Balance at January 1, 2019** | **(21)** |
| **Purchases** | **(9)** |
| **Changes in profit or loss** | |
| **Mark-to-market** | **(5)** |
| **Settlements** | **26** |
| **Total** | **21** |
| **Balance at December 31, 2019** | **(9)** |

| *(millions of Canadian dollars)* | Level 3 |
|---|---|
| Balance at January 1, 2018 | (31) |
| Purchases | (21) |
| Changes in profit or loss | |
| Mark-to-market | (18) |
| Settlements | 49 |
| Total | 31 |
| Balance at December 31, 2018 | (21) |

## 24. RELATED PARTY TRANSACTIONS

Hydro enters into various transactions with its parent 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 Hydro transacts are as follows:

| Related Party | Relationship |
|---|---|
| Nalcor | 100% shareholder of Hydro |
| Churchill Falls | Joint arrangement of Hydro |
| The Province | 100% shareholder of Nalcor |
| Twin Falls | Joint venture of Churchill Falls |
| Energy Marketing | Wholly-owned subsidiary of Nalcor |
| Hydro-Québec | 34.2% shareholder of Churchill Falls |
| Labrador-Island Link Operating Corporation (LIL Opco) | Wholly-owned subsidiary of Nalcor |
| Lower Churchill Management Corporation | Wholly-owned subsidiary of Nalcor |
| Nalcor Energy – Bull Arm Fabrication Inc. | Wholly-owned subsidiary of Nalcor |
| Nalcor Energy – Oil and Gas Inc. | Wholly-owned subsidiary of Nalcor |
| PUB | Agency of the Province |
| The Trust | Created by the Province with Churchill Falls as the beneficiary |

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 settlement within 30 days, unless otherwise stated.

(a) For the year ended December 31, 2019, Lower Churchill Management Corporation contributed $0.7 million (2018 - $1.7 million) in additions to property, plant and equipment.

(b) 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 2019, Hydro incurred $2.1 million (2018 - $1.9 million) in costs related to the PUB and has included $0.7 million (2018 - $0.7 million) in trade and other payables.

(c) As at December 31, 2019, Hydro has a payable to related parties of $7.2 million (2018 - $7.4 million) and a receivable from related parties for $16.3 million (2018 - $18.0 million). This payable/receivable consists of various intercompany operating costs and power purchases.

(d) The debt guarantee fee for 2019 was $8.6 million (2018 - $6.9 million). It was paid to the Province on March 26, 2019.

(e) For the year ended December 31, 2019, Hydro recovered $2.0 million (2018 - $2.0 million) of operating costs from related parties representing the provision of administrative services.

(f) For the year ended December 31, 2019, Hydro incurred costs of $6.7 million (2018 - $5.4 million) in operating costs from related parties representing the provision for administrative services.

(g) For the year ended December 31, 2019, Hydro has purchased $28.0 million (2018 - $28.4 million) of power generated from assets related to Exploits Generation, which are owned by the Province. In addition, Hydro operates these assets on behalf of Nalcor and recovered costs in the amount of $26.2 million (2018 - $30.4 million).

(h) For the year ended December 31, 2019, Hydro has recovered intercompany labour related expenses of $0.6 million (2018 - $0.6 million).

(i) Hydro received $1.0 million (2018 - $0.8 million) from Nalcor associated with the Upper Churchill Redress Agreement to be used to provide a rebate to each residential customer in Innu Communities and to the Mushuau Innu First Nation.

(j) Hydro recorded $2.2 million (2018 - $2.0 million) as an energy rebate from the Province to offset the cost of basic electricity consumption for Labrador rural isolated residential customers under the Northern Strategic Plan. As at December 31, 2019, there is a balance of $0.4 million (2018 - $0.4 million) outstanding in trade and other receivables.

(k) Hydro received $nil (2018 - $0.4 million) from other lines of business as a contribution in aid of construction for Information Systems assets.

(l) During 2019, Churchill Falls generated revenue from Hydro-Québec of $95.3 million (2018 - $94.8 million) and Hydro has recognized its share of $62.7 million (2018 - $62.4 million).

(m) Under the terms of 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, 2019, $6.9 million (2018 - $6.7 million) was payable to the Province. Hydro has recognized its share of $4.5 million (2018 - $4.4 million).

(n) On March 14, 2018, Hydro issued new long-term debt, Series 1A, with face value of $300.0 million. The Province issued the debt specifically on Hydro's behalf and lent the proceeds to Hydro.

(o) On December 19, 2019, Hydro purchased a 138/25 kV Transformer from Muskrat Falls for $0.7 million.

(p) Hydro recorded $nil (2018 - $1.4 million) as a receivable from Lower Churchill Management Corporation to reimburse costs of running the Holyrood Gas Turbine to accommodate the interconnection of Soldier's Pond.

**24.1 Key Management Personnel Compensation**

Compensation for key management personnel, which Hydro defines as its executives who have the primary authority and responsibility for 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 in the amount of $0.2 million (2018 - $0.2 million).

| *For the year ended December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Salaries and employee benefits | **2** | 2 |

## 25. COMMITMENTS AND CONTINGENCIES

(a) Hydro has 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 that Hydro's exposure to such claims and litigation, to the extent not covered by insurance policies or otherwise provided for, is not expected to materially affect its financial position.

(b) Outstanding commitments for capital projects total approximately $16.7 million as at December 31, 2019 (2018 - $35.0 million).

(c) 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 kW | 2004 | 15 years |
| Wind | 27 MW | 2008 | 20 years |
| Wind | 27 MW | 2009 | 20 years |
| Wind | 300 kW | 2010 | Continual |
| Hydroelectric | 175 kW | 2019 | 15 years |
| Biomass | 450 kW | 2018 | 1 year post in-service of Muskrat Falls in-service date |

Estimated payments due in each of the next five years are as follows:

| *(millions of Canadian dollars)* | 2020 | 2021 | 2022 | 2023 | 2024 |
|---|---|---|---|---|---|
| Power purchases | 31.4 | 31.1 | 30.8 | 19.5 | 18.6 |

(d) Through a power purchase agreement signed October 1, 2015, with Energy Marketing, Hydro maintains the transmission services contract it entered into with Hydro-Québec TransÉnergie which concludes in 2024.

The transmission rental payments for the next five years are estimated to be as follows:

| | |
|---|---|
| 2020 | $20.6 million |
| 2021 | $21.0 million |
| 2022 | $21.2 million |
| 2023 | $21.4 million |
| 2024 | $21.6 million |

(e) 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 and the ruling required Churchill Falls to pay court costs of approximately $0.4 million to Hydro-Québec. Churchill Falls filed a Notice of Appeal with the Québec Court of Appeal and the appeal hearing was held on December 4, 2018. The decision of the Court of Appeal was issued on June 20, 2019 and the decision of the Québec Superior Court was partially overturned. In addition, the Court of Appeal reversed the order requiring Churchill Falls to pay court costs for the trial and ordered Hydro- Québec to pay Churchill Falls' court costs associated with the Appeal proceedings. The decision of the Court of Appeal was not appealed so this matter is closed. The impact of the ruling is under review by Management.

(f) In 2013, Hydro entered into a Power Purchase Agreement with Muskrat Falls for the purchase of energy and capacity from the Muskrat Falls Plant. The supply period under the agreement is 50 years and commences at the date of commissioning of the Muskrat Falls Plant. Estimated payments for the next five years have not yet been determined.

(g) In 2013, Hydro entered into the Transmission Funding Agreement (TFA) with LIL Opco, in which Hydro has committed to make payments which will be sufficient for LIL Opco to recover all costs associated with rent payments under the LIL Lease and payments to cover operating and maintenance costs incurred by LIL Opco. Hydro will be required to begin mandatory payments associated with the TFA upon commissioning of the Lower Churchill Project assets. The term of the TFA is anticipated to continue until the service life of the LIL assets has expired.

(h) In 2018, Hydro entered into three additional agreements in order to enable transmission of energy from Labrador to the island; the Labrador Island Link Interim Transmission Funding Agreement (LIL interim TFA); Labrador Transmission Assets Interim Transmission Funding Agreement (LTA interim TFA); and a Minimum Performance Guarantee (the Guarantee). The LIL Interim TFA is between the Labrador Island Link Limited Partnership (Partnership) and Hydro to provide for cost reimbursement, from Hydro to the Partnership, for operating and maintenance costs resulting from the LIL being made available for service earlier than would otherwise be required. The LTA Interim TFA is between the Labrador Transmission Corporation (LTC) and Hydro to provide for cost reimbursement, from Hydro to LTC, for operating and maintenance costs resulting from the LTA being made available for service earlier than would otherwise be required. Both of the Interim TFA's were developed based on the existing long-term Transmission Funding Agreement, executed in 2013. The Guarantee is between Nalcor Energy and Hydro and provides Hydro with guaranteed minimum average availability of the LIL and LTA during the term of the Interim TFA's. Should performance deficiencies by either or both of the LIL and LTA result in Hydro realizing a net loss from the use of off-island purchases, Nalcor will reimburse Hydro, in proportion to the contribution of these deficiencies to the net loss, for the operating and maintenance costs of the LIL and LTA. No payments have been made to date.

(i) 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 February 2019, Hydro entered into a revised agreement with CBPP that 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 and CBPP. In December 2019, Hydro entered into a revised agreement with Vale that expires in March of 2020.

## 26. CAPITAL MANAGEMENT

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.

The capital managed by Hydro is comprised of debt (long-term debentures, short-term borrowings, bank credit facilities and bank indebtedness) and equity (share capital, shareholder contributions, reserves and retained earnings).

A summary of the capital structure is outlined below:

| *(millions of Canadian dollars)* | **2019** | | 2018 | |
|---|---|---|---|---|
| Sinking funds | **(174)** | | (164) | |
| Short-term borrowings | **233** | | 189 | |
| Current portion of long-term debt | **7** | | 7 | |
| Long-term debt | **1,776** | | 1,784 | |
| | **1,842** | **64.1%** | 1,816 | 64.9% |
| **Equity** | | | | |
| Share capital | **23** | | 23 | |
| Contributed capital | **152** | | 152 | |
| Reserves | **(22)** | | (13) | |
| Retained earnings | **877** | | 822 | |
| | **1,030** | **35.9%** | 984 | 35.1% |
| **Total Debt and Equity** | **2,872** | **100.0%** | 2,800 | 100.0% |

**26.1 Hydro**

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 requiring Hydro to ensure that its consolidated debt to total capitalization ratio does not exceed 85%. As at December 31, 2019, 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. On February 20, 2020, the Lieutenant-Governor in Council issued Order in Council OC2020-18 to increase the level of short-term borrowings permitted by Hydro from $300 million to $500 million, effective until March 31, 2022. As a result, the current limit is now $500.0 million and $233.0 million is outstanding as at December 31, 2019 (2018 - $189.0 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 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; the Province now issues debt in the domestic capital markets, on Hydro Regulated's behalf, and in turn loans the funds to Hydro Regulated on a cost recovery basis. Any additional funding to address long-term capital funding requirements will require approval from the Province and the PUB.

### 26.2 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 increase, 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 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.

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 Bankers' Acceptance (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, 2019 (2018 - $nil).

Churchill Falls has issued three irrevocable letters of credit totaling $2.0 million (2018 - $2.0 million), $1.0 million of which does not impact the borrowing limit of the operating credit facility (2018 - $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.

## 27. SUPPLEMENTARY CASH FLOW INFORMATION

| *For the year ended December 31 (millions of Canadian dollars)* | **2019** | 2018 |
|---|---|---|
| Trade and other receivables | **5** | - |
| Inventories | **(7)** | (1) |
| Prepayments | **(1)** | (1) |
| Trade and other payables | **28** | (46) |
| Changes in non-cash working capital balances | **25** | (48) |
| | | |
| Related to: | | |
| Operating activities | **31** | (25) |
| Investing activities | **(6)** | (23) |
| | **25** | (48) |

## 28. SEGMENT INFORMATION

Hydro operates in four business segments. The designation of segments is based on a combination of regulatory status and management accountability.

Hydro Regulated activities encompass sales of electricity to customers within the Province that are regulated by the PUB. Hydro Non-Regulated activities include the sale of recapture energy, purchased from Churchill Falls, to mining operations in Labrador West as well as costs of Hydro that are excluded from the determination of customer rates. Churchill Falls operates a hydroelectric generating facility which sells electricity to Hydro-Québec and Hydro Regulated. Energy Marketing includes the sale of electricity and transmission to Nalcor Energy Marketing.

| *(millions of Canadian dollars)* | Hydro Regulated | Churchill Falls | Energy Marketing | Non-Regulated Activities | Inter-Segment | Total |
|---|---|---|---|---|---|---|
| | For the year ended December 31, 2019 | | | | | |
| **Energy sales** | **608** | **94** | **5** | **44** | **(31)** | **720** |
| **Other revenue** | **5** | **-** | **21** | **(1)** | **3** | **28** |
| **Revenue** | **613** | **94** | **26** | **43** | **(28)** | **748** |
| **Fuels** | **217** | **-** | **-** | **-** | **-** | **217** |
| **Power purchased** | **84** | **-** | **4** | **42** | **(31)** | **99** |
| **Operating costs** | **136** | **43** | **-** | **5** | **-** | **184** |
| **Transmission rental** | **1** | **-** | **21** | **-** | **-** | **22** |
| **Depreciation and amortization** | **83** | **20** | **-** | **-** | **-** | **103** |
| **Net finance expense (income)** | **91** | **(1)** | **-** | **(1)** | **-** | **89** |
| **Other expense** | **8** | **-** | **-** | **-** | **-** | **8** |
| **Expenses** | **620** | **62** | **25** | **46** | **(31)** | **722** |
| **Preferred dividends** | **-** | **(3)** | **-** | **-** | **3** | **-** |
| **(Loss) profit before regulatory adjustments** | **(7)** | **35** | **1** | **(3)** | **-** | **26** |
| **Regulatory adjustments** | **(37)** | **-** | **-** | **-** | **-** | **(37)** |
| **Profit (loss) for the year** | **30** | **35** | **1** | **(3)** | **-** | **63** |
| **Capital expenditures*** | **129** | **44** | **-** | **-** | **-** | **173** |
| **Total assets** | **2,735** | **647** | **11** | **11** | **-** | **3,404** |

***Capital expenditures include non-cash additions of $0.7 million contributed by Lower Churchill Management Corporation, and $2.0 million of interest capitalized during construction.**

| *(millions of Canadian dollars)* | Hydro Regulated | Churchill Falls | Energy Marketing | Non-Regulated Activities | Inter-Segment | Total |
|---|---|---|---|---|---|---|
| | For the year ended December 31, 2018 | | | | | |
| | | | | | | (Restated - Note 29) |
| Energy sales | 557 | 89 | 7 | 34 | (27) | 660 |
| Other revenue | 7 | - | 21 | - | 3 | 31 |
| Revenue | 564 | 89 | 28 | 34 | (24) | 691 |
| Fuels | 189 | - | - | - | - | 189 |
| Power purchased | 71 | - | 7 | 33 | (27) | 84 |
| Operating costs | 136 | 41 | - | - | 1 | 178 |
| Transmission rental | - | - | 21 | - | - | 21 |
| Depreciation and amortization | 87 | 18 | - | - | - | 105 |
| Net finance expense (income) | 87 | (1) | - | (1) | - | 85 |
| Other expense | 13 | 1 | - | - | - | 14 |
| Expenses | 583 | 59 | 28 | 32 | (26) | 676 |
| Preferred dividends | - | (3) | - | - | 3 | - |
| (Loss) profit before regulatory adjustments | (19) | 33 | - | 2 | (1) | 15 |
| Regulatory adjustments | (47) | - | - | - | - | (47) |
| Profit (loss) for the year | 28 | 33 | - | 2 | (1) | 62 |
| Capital expenditures* | 160 | 43 | - | - | - | 203 |
| Total assets | 2,700 | 615 | 23 | 4 | - | 3,342 |

*Capital expenditures include non-cash additions of $1.7 million contributed by Lower Churchill Management Corporation.

## 29. PRIOR PERIOD ADJUSTMENTS

The December 31, 2018 figures have been restated as a result of a misstatement relating to the inclusion of the sale and purchase of energy between Churchill Falls and Hydro. The year ended December 31, 2018 figures have been restated to reduce energy sales by $24.0 million and to reduce power purchased by $24.0 million.

The following table summarizes the adjustments to the affected accounts from the previously issued annual consolidated financial statements to the current year comparative figures:

| *For the year ended December 31 (millions of Canadian dollars)* | **Previously stated 2018** | **Adjustment 2018** | **Restated 2018** |
|---|---|---|---|
| **Statement of Profit and Comprehensive Income** | | | |
| Energy sales | 684 | (24) | **660** |
| Power purchased | 108 | (24) | **84** |

## 30. SUBSEQUENT EVENT

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