Questions and Answers
Commercial Agreements for the Muskrat Falls Project including Power Purchase Agreement, Financing, Federal Loan Guarantee Agreements and Nalcor’s Financial Operations
Updated August 20, 2014

July 2014

Q1. How will cost overruns on the generation site, the Labrador Island Link and Labrador transmission assets influence the financial participation of Emera and its subsidiaries? What risk will they bear from cost escalation?

A1. Emera does not have an ownership interest in either Muskrat Falls or the Labrador Transmission Assets. With respect to the Labrador-Island Transmission Link, their participation is addressed in the NELDA and LIL LPA executed between Nalcor and Emera in July 2012.

Q2. Did the federal government insist on the regressive amendments to the Electrical Power Control Act that exacerbated the monopoly power of Nalcor, as a condition for the federal loan guarantee?

A2. Certainty is required with respect to cost recovery and cash flow in order to achieve project financing, whether financing is guaranteed by the Government of Canada or provided directly by a lender. Nalcor has been clear on this fact from the onset of the discussion on Muskrat Falls. Without ensuring clarity that funds would be recovered, financing would not be achieved on the terms provided. Through Nalcor and Newfoundland and Labrador demonstrating that this framework would be put in place, Canada agreed to provide the Federal Loan Guarantee which further enhanced the financing terms and will result in a benefit to electricity consumers in the province in excess of $1 billion.

Q3. Did the federal government also insist that demand side management and conservation be attenuated in order to strengthen the demand for electricity and guarantee repayment of the guaranteed loan?

A3. No demands or conditions on the role of demand side management or conservation programs have been imposed. While historically, the benefit of a conservation program has been linked to fuel displacement at Holyrood, going forward the business case would be assessed based on the value conserved energy that could be sold into export markets. While the actual numbers used in analysis of a specific initiative would change, the principles used to assess the merits of that initiative would not.
Q4. Please advise what nominal inflation rate is assumed in DG2 documents filed in the PUB reference, particularly in CA/KPL-Nalcor-27 Rev 1.

A4. Nalcor used a variety of producer price indices to escalate various costs. Each rate was different for major commodity such as labour, steel, concrete, among other items. These escalation indices were purchased from third parties and therefore cannot be disclosed as this is proprietary information.

The nominal inflation rate used for Muskrat Falls rates in CA/KPL-Nalcor-27 Rev 1 was 2%.

Q5. When will the power purchase agreement signed in November 2013 be released publicly?

A5. The Power Purchase Agreement document was publically released with the updated capital cost for the Muskrat Falls Project on June 26, 2014. This document is available online at: http://muskratfalls.nalcorenergy.com/wp-content/uploads/2013/03/Power-Purchase-Agreement_29Nov2013.pdf

Q6. Will this agreement [Power Purchase Agreement] be subject to regulatory oversight by the PUB? If not, why not?

A6. This question was answered by Ed Martin Nalcor’s AGM. Nalcor’s AGM material and information can be viewed at the following link: http://nalcorenergy.com/agm-2014.asp.

Here’s a summary of his response given at the AGM. The costs of Muskrat Falls and the Labrador-Island Link are going into electricity rates. Provincial legislation has been established that ensures the costs of Muskrat Falls are going into the rate base without going through the PUB for approval. Nalcor has been clear on this fact from the onset of the discussion on Muskrat Falls. Prior to construction of the project, we needed certainty in financing.

Q8. Please advise if the PPA rates charged by Nalcor to Newfoundland and Labrador Hydro will be based upon Escalating Real Levelized Energy Cost (see Column 8 of CA/KPL-Nalcor-27) for DG3.

A8. The Muskrat Falls rate charged to Newfoundland and Labrador Hydro will be based on an escalating real levelized energy rate with 2% escalation.

Q9. Does Nalcor pay federal income tax? Does FIT apply equally to earnings from oil and gas and from electrical energy sales?

A9. Nalcor does not pay federal income tax.

Q10. Does Newfoundland and Labrador Hydro pay FIT?

A10. Newfoundland and Labrador Hydro does not pay federal income tax.

Q11. Can Nalcor please confirm if the Muskrat Falls Corporation must pay federal income tax on the profits realised from sales of energy to Newfoundland and Labrador Hydro.

A11. Muskrat Falls does not pay federal income tax.
Q12. Does the Muskrat Falls Corporation have to pay federal tax on the profits realised from the sales of energy to third parties (Emera or other customers)?
A12. As noted in A11 above, Muskrat Falls does not pay federal income tax.

Q13. Does the transmission company (Jointly owned between Nalcor and Emera) have to pay federal taxes?
A13. The Labrador-Island Link Limited Partnership (LIL LP) is jointly held by two limited partners, Labrador-Island Link Holding Corporation (a Nalcor entity) and ENL Island Link Incorporated (an Emera entity). Earnings in LIL LP would be distributed to its partners, who would then be responsible for any related tax implications. Labrador-Island Link Holding Corporation does not pay federal income tax.

Q14. Does the reference to $30 Billion returned to the provincial government as dividends consider the federal income tax?
A14. The Muskrat Falls Project will generate significant value and cash flows for our province – around $30 billion in nominal value over the life of the project. This value includes the return on and return of equity to the province and considers federal income tax.

Q15. Are all of these revenues sourced from the electric power activities of Nalcor or do they include oil and tax revenues?
A15. No revenue or dividends from Nalcor’s other lines of business, including Nalcor Oil and Gas have been included in the $30 billion.

April 2014

Q1. How will the project be financed if project costs exceed the limit imposed for the federal loan guarantee?
A1. The guaranteed debt amount is capped at $5 billion. Costs above this amount will be funded through equity or additional non-guaranteed debt in accordance with the provisions of the November 2012 Federal Loan Guarantee Agreement which remains available on the newsroom/reports section on the project website. With respect to equity, it will be provided solely by Nalcor/Government of Newfoundland and Labrador (GNL) for the Muskrat Falls and Labrador Transmission Assets components of the project, and by Nalcor/GNL and Emera in proportion to their ownership interests for the Labrador-Island Link. This is in accordance with the provisions of the Equity Agreements and the Newfoundland and Labrador Development Agreement, which is also available online.

Q2. What recourse does the federal government have in the event of default?
A2. Similar to any secured lender, in the event of a default that cannot be cured under the provisions of the project finance arrangements, the federal government has the ability to exercise its security interest and assume control of the financed assets.
Q3. What commitments have been made to the federal government for which the province is liable?

A3. The province has agreed to maintain the conditions necessary for the project to be built and costs recovered from electricity customers, thus maintaining the certainty required for the federal loan guarantee. This is addressed in the Intergovernmental Agreement which is also publicly available on the project’s website.

March 2014

Q1. Article 3.5B of the Federal Loan guarantee identifies conditions precedent to the execution and delivery of the loan guarantee. Article 3.5B (ix) calls for Review of technical aspects of the Projects, including engineering, water resource and other required due diligence by the Independent Engineer (as defined herein) and preparation and finalization (as confirmed by the Guarantor and Lenders, acting reasonably) of a technical due diligence report (the “IE DD Report”) confirming that the Project execution plans are commercially reasonable, and consistent with Good Utility Practice;” Please identify the Independent Engineer. Who are they and how were they selected, and by whom?

A1. In accordance with the terms and conditions of the November 2012 Federal Loan Guarantee (FLG) Agreement, MWH Canada was engaged as the independent engineer for the Government of Canada (Canada), in its capacity as guarantor, to assist in Canada’s due diligence of the Muskrat Falls Project. Following the required technical review, MWH issued an independent engineer report to Canada to facilitate satisfaction of the related condition precedent found in section 3.5 of the FLG Agreement. Canada subsequently issued the FLG which then allowed $5.0 billion of Canada guaranteed, AAA-rated long-term bonds to be issued for the Muskrat Falls Project on December 10, 2013.

Q2. In response to my previous question in June for access to the Report of the Independent Engineer you advised that the report was “commercially sensitive”. The Nova Scotia Utility and Review Board has ordered that the reports of the Independent Engineer concerning the Maritime Link be filed with the Board. In order to provide residents of Newfoundland and Labrador with the same level of transparency as Nova Scotia Power is providing to the residents of Nova Scotia will Nalcor reconsider its position on the release of reports of the Independent Engineer?

A2. Nalcor received the independent report from the Government of Canada on Friday, February 21, 2014, and we are taking the time to thoroughly review the document. While it is likely that significant portions of this report will be released, we still need time to review the entire report and make a determination as to what information is deemed commercially sensitive in nature. In making that determination, Nalcor considers established legislation to guide that decision on the release of information. Additionally, since the report was completed on behalf of the Government of Canada, we need to consult with them on the release of its report in whole or in part.

Q3. In Nalcor’s Benefit report for November upcoming requests for proposals include CH008 for Construction of North Spur Stabilization Works. Please describe the scope of this project and
how these works will deal with the instability created by potential liquefaction of quick clay on the North Spur. The concerns that have been publically raised about the north spur have been addressed through engineering feasibility studies. The geotechnical conditions at the North Spur are well understood with the final details being confirmed following a field program completed this year. Nalcor is confident in the approach for the North Spur and the cost estimate for this was included in the DG3 project estimate.

In 2013, AMEC Environment and Infrastructure completed the geotechnical field investigation services at the north spur, which included sonic and conventional boreholes, in situ and laboratory testing, installation of instrumentation and surveys. We published information and a technical presentation on October 31, 2013. While technical in nature, this presentation outlines the stabilization work for the North Spur. This information can be found at: http://blog.nalcorenergy.com/lower-churchill-project-north-spur-stabilization-works-2/

Stabilization work on the north spur at Muskrat Falls will be completed prior to impoundment, which will take place in the later years of construction of the Muskrat Falls hydroelectric generating facility.


Q4. The following quote is from the December 10, 2013 backgrounder:

Request for Financing (RFF)
On May 31, 2013, Nalcor issued a RFF, inviting major financial institutions to provide proposals for the role of Lead Arranger in which they would provide a fully underwritten financing commitment for $5 billion of debt financing that would be funded at financial close. On October 1, Nalcor received fully underwritten proposals from a variety of financial institutions and began a comprehensive evaluation process that also involved Provincial and Federal Government representatives.

On November 6, Nalcor appointed TD Securities and Goldman Sachs as Co-Lead Arrangers. The Lead Arrangers, along with a syndicate of financial institutions, (including BMO Nesbitt Burns, CIBC World Markets, RBC Dominion Securities, Scotia Capital, HSBC, Bank of America Merrill Lynch, Beacon Securities, Casgrain & Company, Desjardins Securities, Laurentian Bank, and National Bank Financial) then proceeded to raise $5 billion through the debt capital markets. On December 9, the financing was formally launched and, following a global marketing effort, the Lead Arrangers priced the $5 billion financing on December 10. Closing for the bonds will be December 13, 2013.

Will the financing be solely through the sale of bonds and, if so, will they be sold to institutions only or will the Arrangers and syndicate also offer them to private individuals?

A4. Information to answer this question is provided in the Offering Circular dated December 10, 2013 and is available on the Muskrat Falls Project website at: http://muskratfalls.nalcorenergy.com/wp-content/uploads/2014/03/MFLTA-LIL-Funding-Trust-Final-Offering-Circular-Dec-10-2013.pdf
Q5.  What were the consultancy/legal/underwriting fees associated with this transaction? What are the net proceeds to Nalcor from this financing?
A5.  Information to answer this question is provided in the Offering Circular dated December 10, 2013 and is available on the Muskrat Falls Project website at: http://muskratfalls.nalcorenergy.com/wp-content/uploads/2014/03/MFLTA-LIL-Funding-Trust-Final-Offering-Circular-Dec-10-2013.pdf

Q6.  Will the bonds be denominated in Canadian dollars?

Q7.  Will bonds be offered to lenders throughout the world and will there be specific target markets?

Q8.  Has all of the money been raised and will interest obligations for the full financing begin as of December 13, 2013, the Closing date or will borrowing be staggered to match project expenditures?
A8.  Information to answer this question is provided in the Offering Circular dated December 10, 2013 and is available on the Muskrat Falls Project website at: http://muskratfalls.nalcorenergy.com/wp-content/uploads/2014/03/MFLTA-LIL-Funding-Trust-Final-Offering-Circular-Dec-10-2013.pdf

Q9.  What is the interest rate on the bonds/loans? How is the interest rate calculated (daily, monthly, quarterly or annually)? Is there a balloon payment? Does the rate vary during the term of the loan? Will interest and principal be blended to equalize payments? Is there a requirement for a sinking fund and what are the obligations under such a fund?

Q10. Does the bond/loan come under the legal jurisdiction of the province of NL? What event(s) constitutes default? And under default provisions of the loan does the interest rate rise?
A10. Information to answer this question is provided in the Offering Circular dated December 10, 2013 and is available on the Muskrat Falls Project website at: http://muskratfalls.nalcorenergy.com/wp-content/uploads/2014/03/MFLTA-LIL-Funding-Trust-Final-Offering-Circular-Dec-10-2013.pdf
Q11. Have there been any changes/revisions to the Federal Loan Guarantee (FLG) since it was signed? Are the loan amounts for each project (Muskrat Falls, the Labrador/Island link and the Maritime link) consistent with the FLG?

Q12. Has the loan or any part thereof been drawn down by Nalcor? If so, how is the residual unexpended balance invested until the money is needed? What is the return? At what date did interest start to accumulate on the loan?
A12. The proceeds of the $5.0 billion Muskrat Falls Project bond issuance were invested in a structured deposit product through TD Securities. Given the funding profile and liquidity requirements associated with construction of the Project, this was determined by Nalcor and TD Securities to be the most effective investment strategy.

Q13. When is it anticipated that the Government of Canada and the Province of Newfoundland will finalize the land use agreement for joint management of the Strait of Belle Isle pursuant to the following, also from the December 10, 2013 Backgrounder, and when the corresponding agreement with Nova Scotia will be finalized with respect to the Cabot Strait?
A14. The Government of Newfoundland and Labrador will enter into a land use agreement with the Government of Canada to provide the necessary land rights to the subsea of the Strait of Belle Isle to the Nalcor subsidiary for the installation and operation of transmission cables as part of the Labrador-Island Link. The Government of Newfoundland and Labrador will also enter into an Agreement with the Government of Canada which provides for the joint management of the land use agreement for the Strait of Belle Isle.

It is anticipated that the land use agreements will be finalized during the first half of 2014.

Q15. Will the finalization of these land use agreements delay the two Strait cable crossings?
A16. Both the Labrador-Island Transmission Link and the Maritime Link have been released from environmental assessment, and conditions precedent for the Federal Loan Guarantee and financial close have been achieved. Finalizing the land use agreements by the first half of 2014 will not cause any delay in these projects.

January 2014

Q1. Article 4.9 of the Federal Loan Guarantee provide that The IE shall review the Project documents and any information provided in support of any drawdown requested by a Borrower and shall make a recommendation to the Lender by way of an IE certificate. The Independent Engineer shall be assigned a scope of responsibility designed to ensure the Projects are developed, maintained, and operated in a manner which is consistent with Good Utility Practice (as defined herein).

What is the scope of responsibility of the Independent Engineer and does it include reporting on the financial and arrangements with SNC Lavalin for their EPCM services on the Muskrat Falls project?
A1. In accordance with the terms and conditions of the November 2012 Federal Loan Guarantee Agreement, MWH Canada Inc. (MWH) was engaged as the independent engineer (IE) for the Government of Canada (Canada), in its capacity as guarantor, to assist in Canada's due diligence of the Muskrat Falls Project. Following the required technical review, MWH issued an independent engineer report to Canada in November 2013 to facilitate satisfaction of the related condition precedent of the Federal Loan Guarantee Agreement.

The IE will be in place for the duration of the construction phase and into the operations phase of the project. Phase 1 of the IE agreement was for the pre-financial close phase of the project. This work provided satisfaction to Canada prior to issuing a federal loan guarantee to back the $5 billion financing for the Muskrat Falls Project. Phase 2 of the IE agreement commenced with financial close in December 2013 and includes oversight of project construction/operations. MWH will serve in an oversight and monitoring capacity on behalf of Canada through the construction and operating phases of the project.

Q2. The following is quoted from the background information released on December 10, 2013 when the Premier announced financing for the Muskrat Falls project: 

In exchange for providing the Federal Loan Guarantee for the financing, Canada requested binding confirmation of these equity commitments. To satisfy this commitment, the Province and Nalcor are providing separate agreements and guarantees for each aspect of the project. With the Newfoundland and Labrador Equity Support Agreements, Nalcor is entering into a separate Agreement for each component of the Muskrat Falls Project for the provision of base and contingent equity to each subsidiary. Nalcor will commit to provide base equity to its subsidiaries sufficient to meet the budgeted debt-to-equity ratios for each component of the project, and contingent equity for any further costs to achieve commissioning.

Please define base and contingent equity and advise how much of each will be provided to each subsidiary. Please advise as to how Nalcor will source this “base” and “contingent” equity.

A2. As noted in your statement above, this is the definition of base and contingent equity “Nalcor will commit to provide base equity to its subsidiaries sufficient to meet the budgeted debt-to-equity ratios for each component of the project, and contingent equity for any further costs to achieve commissioning.”


Q3. The aforementioned release of December 10, 2010 also states:

The Government of Newfoundland and Labrador is guaranteeing the Equity Support Agreements through the Newfoundland and Labrador Equity Support Guarantees. The Province is entering into a separate agreement for each component of the project to guarantee the payment of Nalcor’s equity commitments should Nalcor fail to fulfill its commitments.

Please provide a copy of each of the Equity Support Agreements.

A3. The Equity Support Agreements are available online at: [https://muskratfalls.nalcorenergy.com/newsroom/reports/](https://muskratfalls.nalcorenergy.com/newsroom/reports/)
Q4. Reference is made in the release to savings in interest costs of $1 Billion. How is this calculated?
A4. The $1 billion in interest savings is the difference in total financing we would have received versus the guaranteed financing we received.

Q5. The value of the Canadian dollar has declined significantly over the past year. To what extent does this affect the DG3 numbers? What portion of the DG3 budget was estimated to be spent outside Canada? Have there been any hedging activities/forward currency contracts to mitigate any additional costs as a result of Canadian currency depreciation?
A5. The Canadian dollar has declined approximately eight per cent since May of 2013. While the DG3 estimate would be unaffected by this change, any difference between exchange rates on the date of transactions and the assumption used in the DG3 estimate would affect outturn capital costs.
   Even though significant purchases are being made outside Canada, many were priced in Canadian dollars with foreign exchange and commodity prices locked in at the date of contract execution.
   With most purchasing for the project completed, the risks inherent in a hedging or forward currency purchase strategy did not warrant embarking on such a program.

Q6. How will devaluation impact on debt repayment, particularly on debt borrowed in other countries and possibly denominated in foreign currencies?
A6. There will be no impact as all funds are borrowed in Canadian dollars.

November 2013

Q1. When do you anticipate “financial close” will take place for the purposes of the federal loan guarantee?
A1. Nalcor started its request for financing process for $5 billion in debt financing for the Muskrat Falls Project in June 2013 and major Canadian and global financial institutions were invited to submit proposals. This is a robust, competitive process and it has progressed as planned with considerable, positive interest from potential lenders. Through the Federal Loan Guarantee, this debt financing will benefit from Canada’s AAA credit rating. Nalcor has received competitive proposals and they are currently being evaluated.
   Given the size of this debt financing transaction, we are careful and prudent not to release any details prior to the placement of financing that could impact financial market rates and conditions and adversely affect the people of NL for the next 50 years.