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**Highway 104 Western
Alignment Corporation
Financial Statements**
March 31, 1998

Contents

	<u>Page</u>
Auditors' Report	1
Statements of Loss and Deficit	2
Balance Sheet	3
Statement of Changes in Financial Position	4
Notes to the Financial Statements	5 - 11

Auditors' Report

To the Shareholder of Highway 104
Western Alignment Corporation

We have audited the balance sheet of Highway 104 Western Alignment Corporation as at March 31, 1998, and the statements of loss and deficit and changes in financial position for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

Except as explained in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

As a result of system deficiencies with the Tolling System, we were unable to obtain sufficient evidence with respect to the completeness of operating revenue and the customer account balances for the four month period ended March 31, 1998. Consequently, we were unable to determine whether any adjustments might be necessary to the operating revenue and customer account balances presented in the financial statements.

In our opinion, except for the effect of adjustments, if any, which we might have determined to be necessary had we been able to obtain sufficient evidence regarding the completeness of operating revenue and customer account balances as explained in the previous paragraph, these financial statements present fairly, in all material respects, the financial position of the Corporation as at March 31, 1998, and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Halifax, Canada
August 14, 1998

Grant Thornton

Chartered Accountants

Highway 104 Western Alignment Corporation

Statements of Loss and Deficit

Four Months Ended March 31

1998

Revenue	
Facility revenue	\$ 2,705,173
Interest income	<u>166,391</u>
	<u>2,871,564</u>
Expenses	
Bondholder representative fees	13,333
Trustee fees	13,118
Salaries and benefits	51,682
Office	18,786
General and administrative	54,146
Enforcement	20,000
Independent engineer	1,753
Routine maintenance	216,668
Facility operations	430,902
Transponders	<u>225,563</u>
	<u>1,045,951</u>
Earnings before other items	1,825,613
Other items	
Government assistance amortization (Note 2)	277,450
Amortization and depreciation	(660,894)
Interest on line of credit	(389,260)
Interest on long term debt	<u>(2,727,547)</u>
Net loss	\$ <u>(1,674,638)</u>
<hr/>	
Retained earnings, beginning of period	\$ Nil
Net loss	(1,674,638)
Transfer to reserve for restricted assets (Note 12)	<u>(1,908,808)</u>
Deficit, end of period	\$ <u>(3,583,446)</u>

See accompanying notes to the financial statements.

Highway 104 Western Alignment Corporation

Balance Sheet

March 31 1998 1997

Assets

Project bank account	\$ 1,095,535	\$
Inventory	12,137	
Prepays (Note 3)	214,029	
Receivables (Note 4)	1,198,583	196,962
Loan receivable (Note 5)		3,507,612
Restricted assets (Note 6)	7,929,146	8,102,788
Facility (Note 7)	123,585,732	84,761,733
Deferred costs (Note 8)	<u>1,280,017</u>	<u>900,978</u>
	<u>\$ 135,315,179</u>	<u>\$ 97,470,073</u>

Liabilities

Payables and accruals	\$ 1,168,717	\$ 1,096,616
Deferred revenue	260,090	
Long term debt (Note 10)	80,288,098	67,373,456
Payable to the Province of Nova Scotia (Note 11)	250,000	
Deferred government assistance (Note 2)	<u>55,022,911</u>	<u>29,000,000</u>
	<u>136,989,816</u>	<u>97,470,072</u>

Shareholders' Deficiency

Capital stock, one no par value share issued and outstanding in favour of the Province of Nova Scotia	1	1
Reserve for restricted assets (Note 12)	1,908,808	
Deficit	<u>(3,583,446)</u>	<u>1</u>
	<u>(1,674,637)</u>	<u>1</u>
	<u>\$ 135,315,179</u>	<u>\$ 97,470,073</u>

Commitments and contractual obligations (Note 15)

On behalf of the Board

_____ Director

See accompanying notes to the financial statements.

Highway 104 Western Alignment Corporation

Statement of Changes in Financial Position

Year Ended March 31

1998

1997

Cash derived from (applied to)

Operating		
Net loss	\$ (1,674,638)	\$
Government assistance amortization	(277,450)	
Amortization of deferred financing fees	11,800	
Amortization and depreciation	<u>660,894</u>	<u> </u>
	(1,279,394)	
Change in non-cash operating working capital (Note 13)	<u>2,612,016</u>	<u>(2,607,958)</u>
	<u>1,332,622</u>	<u>(2,607,958)</u>
Financing		
Issue of common share		1
Increase in long term debt	12,914,642	67,373,456
Government assistance	26,300,361	29,000,000
Advance from Province of Nova Scotia	<u>250,000</u>	<u> </u>
	<u>39,465,003</u>	<u>96,373,457</u>
Investing		
Decrease (increase) in restricted assets	173,642	(8,102,788)
Construction of facility	(39,446,933)	(84,761,733)
Deferred costs - financing fees		(760,368)
Deferred costs - start up	<u>(428,799)</u>	<u>(140,610)</u>
	<u>(39,702,090)</u>	<u>(93,765,499)</u>
Net increase in cash	1,095,535	
Cash		
Beginning of year	<u>Nil</u>	<u> </u>
End of year	<u>\$ 1,095,535</u>	<u>\$ Nil</u>

See accompanying notes to the financial statements.

Highway 104 Western Alignment Corporation

Notes to the Financial Statements

March 31, 1998

1. Nature of operations

The Corporation has been established for the purpose of financing, design, construction, operation and maintenance of the Facility consisting mainly of a 45 km stretch of highway (referred to as the Highway 104 Western Alignment) between Masstown and Thomson Station in the Counties of Colchester and Cumberland, Nova Scotia.

2. Summary of significant accounting policies

Pre-operating and operating periods

The pre-operating period was the twenty month construction period commencing April 1, 1996 until the date of acceptance in November 1997. Operations began December 1, 1997.

Facility

The Facility consists of the highway referred to as the Highway 104 Western Alignment and the toll plaza constructed on the highway. The costs of the facility include certified progress payments to the Facility's contractor, independent engineer fees, professional fees and interest costs incurred during the pre-operating period. These costs are being amortized over thirty years commencing at the start of the operating period using the sinking fund method with an annual compounding rate of 5%.

Deferred costs - start up

Administrative expenses incurred during the pre-operating period have been deferred as start-up costs and are being amortized to operations, on a pro-rata basis, over a five year period commencing at the start of the operating period.

Deferred costs - financing fee

Financing, commitment and bondholder representative fees related to the establishment and placement of the senior and junior toll revenue bonds have been deferred and are being amortized to operations over the term of the related bond debt commencing at the start of the operating period.

Deferred government assistance

Government assistance provided by the Province of Nova Scotia has been recorded as a deferral and is being amortized to operations over thirty years commencing at the start of the operating period using the sinking fund method with an annual compounding rate of 5%.

Highway 104 Western Alignment Corporation

Notes to the Financial Statements

March 31, 1998

3. Prepays	1998	1997
Operating expenses	\$ 50,421	\$
Advance to operator	<u>163,608</u>	<u> </u>
	<u>\$ 214,029</u>	<u>\$</u>

4. Receivables	1998	1997
Final contract adjustments	\$ 174,795	\$
Provincial contribution (Note 9)	675,637	
Provincial supplemental payments	214,052	
Interest		196,962
Harmonized Sales Tax	<u>134,099</u>	<u> </u>
	<u>\$ 1,198,583</u>	<u>\$ 196,962</u>

5. Loan receivable

Mobilization loan advanced to Atlantic Highway Corporation, non-interest bearing and repayable at a rate of 10% of certified progress payments repaid during the year.

6. Restricted assets			1998	1997
	Cash	Investments	Total	Total
Construction account	\$ 20,338	\$	\$ 20,338	\$ 7,602,498
Senior debt service reserve account	337	5,636,429	5,636,766	500,290
Capital reserve account	319	1,763,989	1,764,308	
Major maintenance reserve account	<u>622</u>	<u>507,112</u>	<u>507,734</u>	
	<u>\$ 21,616</u>	<u>\$ 7,907,530</u>	<u>\$ 7,929,146</u>	<u>\$ 8,102,788</u>

Investments are recorded at cost, have a weighted average term of 8.46 months to maturity and a weighted average interest rate of 4.94%. The market value of the investments approximates the carrying value.

The following restricted accounts have been established in accordance to trust indenture agreements between the Corporation and the senior and junior bondholders and an Omnibus Agreement between the Corporation and the Province of Nova Scotia:

Highway 104 Western Alignment Corporation

Notes to the Financial Statements

March 31, 1998

6. Restricted assets (continued)

(i) The construction trust account included funds held in trust, in accordance with the Construction Trust Agreement, for the benefit of the Corporation and were eligible for withdrawal based on approved payment directives and certified progress payment requests. The residual funds will be transferred to the project bank account.

(ii) The capital reserve account has been established to provide funds to pay the interest and principal on the senior and junior bonds and the subordinated notes. These funds are also available to pay the trustee and bondholders' representative fees to the extent they are not paid out of the project account. This account provides funding to the major maintenance reserve and the senior debt reserve accounts. The capital reserve account is funded from excess funds transferred from the project bank account of the Corporation.

(iii) The senior debt reserve account has been established to provide a reserve of funds to be available for payments as they come due for the senior toll revenue bonds. Funds can only be transferred from this fund when funds in the capital reserve account are insufficient to pay senior toll revenue bond payments. The account should maintain sufficient reserves equal to 12 months principal and interest payments due on the senior toll revenue bonds. The replenishment of the reserve comes from the capital reserve account.

(iv) The major maintenance reserve account has been established for the purpose of paying major maintenance repair and rehabilitation expenses. This reserve is funded from the capital reserve account in accordance with a maintenance budget recommended by the Independent Engineer through the terms of the major maintenance reserve fund agreement.

7. Facility			<u>1998</u>	<u>1997</u>
	<u>Cost</u>	<u>Accumulated Depreciation</u>	<u>Net book Total</u>	<u>Net book Total</u>
Facility	\$124,208,666	\$ 622,934	\$ 123,585,732	\$ 84,761,733

8. Deferred costs			<u>1998</u>	<u>1997</u>
Start up			\$ 531,449	\$ 140,610
Financing fees			<u>748,568</u>	<u>760,368</u>
			\$ <u>1,280,017</u>	\$ <u>900,978</u>

104 Western Alignment Corporation

Notes to the Financial Statements

March 31, 1998

9. Offset of asset and liability

Pursuant to the Omnibus Agreement with the Province of Nova Scotia, the Corporation has drawn on the Provincial line of credit. The outstanding balance on the line of credit has been repaid on April 15, 1998, with a contribution receivable from the Province of Nova Scotia. The Provincial contribution receivable has been offset by the outstanding balance of the Provincial line of credit in the financial statements. The values of the offset amounts at March 31, 1998 are as follows:

	<u>1998</u>
Provincial contribution receivable	\$ 26,000,000
Provincial line of credit	<u>(25,324,363)</u>
	<u>\$ 675,637</u>

The Provincial line of credit bears interest at a rate of 4.5% per annum.

10. Long term debt	<u>1998</u>	<u>1997</u>
Senior toll revenue bonds bearing interest at 10.13%, maturing March 31, 2026, repayable in partial interest payments from June 30, 1998 until March 31, 2006 and then 80 equal blended quarterly payments of interest and principal of \$2,251,191. Interest from the date of issue has been capitalized as part of the principal and will continue to be capitalized until June 30, 1998. As security, the Corporation has provided an assignment of all the present and future property and assets, including rights to operate the Facility, a security interest in the Debt Service Reserve Account and the Major Maintenance Reserve Account.	\$ 62,293,389	\$ 56,364,537
Junior toll revenue bonds bearing interest at 10.76%, maturing March 31, 2011, repayable in interest payments only from June 30, 1998 until March 31, 2001 and then 40 equal blended quarterly payments of principal and interest of \$503,395. Interest from the date of issue has been capitalized as part of the principal and will continue to be capitalized until June 30, 1998. As security, the Corporation has assigned a second charge security interest in all security pledged to senior toll revenue bondholders.	12,242,063	11,008,919

Highway 104 Western Alignment Corporation

Notes to the Financial Statements

March 31, 1998

10. Long term debt (continued) 1998 1997

Subordinated notes bearing interest at 13.4%, interest only is payable monthly out of excess cash, to the extent it is not paid, it will be compounded semi-annually in arrears, quarterly principal repayments are to begin when surplus cash is available. The notes are expressly subordinated and postponed in right of payment to the senior toll revenue bonds and the junior toll revenue bonds.

<u>5,752,646</u>	
<u>\$ 80,288,098</u>	<u>\$ 67,373,456</u>

Principal repayments will begin in year 2002 and are as follows:

2002	\$ 725,000
2003	806,000

11. Payable to the Province of Nova Scotia

On the date of acceptance, the Province advanced \$250,000 to the Corporation to facilitate the Provincial subsidy. Under the First Amendment to the Omnibus Agreement, the Province reduced the tolls for transponder users and created a Provincial subsidy payable to the Corporation to offset the reduction. The advance is to be repaid to the Province on the earlier of the date when the toll rates are increased back to the original rates laid out in the Omnibus Agreement or when the Corporation has fully extinguished its obligations under the Senior and Junior Bond Indentures.

12. Reserve for restricted assets

The capital reserve account is to be funded from excess funds in the Project Bank Account. In addition, any interest earned on restricted assets should form part of the reserve account. To date, \$1,908,808 has been transferred from operations of the Corporation.

13. Change in non-cash operating working capital 1998 1997

Inventory	\$ (12,137)	\$
Prepays	(214,029)	
Receivables	(1,001,621)	(196,962)
Loan receivable	3,507,612	(3,507,612)
Payables and accruals	72,101	1,096,616
Deferred revenue	<u>260,090</u>	
	<u>\$ 2,612,016</u>	<u>\$ (2,607,958)</u>

Highway 104 Western Alignment Corporation

Notes to the Financial Statements

March 31, 1998

14. Uncertainty due to the Year 2000 Issue

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date.

The effects of the Year 2000 Issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant systems failure which could affect an entity's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the entity, including those related to the efforts of customers, suppliers, or other third parties, will be fully resolved.

15. Commitments and contractual obligations

The Corporation has entered into the following agreements to finance, design, construct, operate and maintain the Highway 104 Western Alignment:

- **Omnibus Agreement**

Agreement dated April 1, 1996, between the Corporation, the Contractor, the Operator and the Province of Nova Scotia to design, finance, construct, operate and maintain the Highway 104 Western Alignment. This agreement acknowledges that the Corporation has entered into a Design Build Agreement and an Operating Agreement to fulfil its obligations to the Province.

Under this agreement, the Province of Nova Scotia retains ownership of the Facility, however, the Corporation is granted the right to operate and collect tolls for a thirty year period, at which time this right will revert back to the Province.

The Province will contribute \$55,000,000 payable as follows: the first \$29,000,000 available April 1, 1996 was released for payment of progress payments; and, the second \$26,000,000 will be available after April 15, 1998 and will be paid to the Corporation only for purposes of repaying the Credit Facility detailed in Note 9 or for paying costs of construction.

- **Operating Agreement**

Agreement dated May 22, 1996 between the Corporation and Atlantic Highways Management Corporation (the Operator) whereby the Operator is required to operate the Facility which includes the toll collection system, toll plaza and the administration building.

Highway 104 Western Alignment Corporation

Notes to the Financial Statements

March 31, 1998

15. Commitments and contractual obligations (continued)

Operator compensation is based on the annual operating budget plus a variable fee, subject to adjustment under certain conditions, equal to 10% of the total annual budget.

- **Major Maintenance Reserve Fund Agreement**

Agreement between the Corporation, the Trustee and the Bondholders' Representative to provide for the major maintenance work required during the operating period of the Facility. The Agreement requires the Corporation, on an annual basis, to engage an independent engineer to report on all major maintenance work to be completed in the upcoming year, as well as a major maintenance budget to determine the required annual amount to be deposited in the Major Maintenance Reserve Account.

- **Annual Roadway Maintenance Agreement**

Five year agreement between the Corporation and the Department of Transportation and Public Works of the Province of Nova Scotia to provide annual roadway maintenance services for an annual fee of \$650,000 commencing April 1, 1998 and subsequently adjusted thereafter for inflation.