

STATEMENT OF MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL INFORMATION

Ontario Power Generation Inc.'s ("OPG") management is responsible for presentation and preparation of the annual consolidated financial statements and Management's Discussion and Analysis ("MD&A").

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and the requirements of the Ontario Securities Commission ("OSC"), as applicable. The MD&A has been prepared in accordance with the requirements of securities regulators, including National Instrument 51-102 of the Canadian Securities Administrators and its related published requirements.

The consolidated financial statements and information in the MD&A necessarily include amounts based on informed judgments and estimates of the expected effects of current events and transactions with appropriate consideration to materiality. Something is considered material if it is reasonably expected to have a significant impact on the Company's earnings, cash flow, value of an asset or liability, or reputation. In addition, in preparing the financial information we must interpret the requirements described above, make determinations as to the relevancy of information to be included, and make estimates and assumptions that affect reported information. The MD&A also includes information regarding the impact of current transactions and events, sources of liquidity and capital resources, operating trends, risks and uncertainties. Actual results in the future may differ materially from our present assessment of this information because future events and circumstances may not occur as expected.

In meeting our responsibility for the reliability of financial information, we maintain and rely on a comprehensive system of internal control and internal audit, including organizational and procedural controls and internal controls over financial reporting. Our system of internal controls includes written communication of our policies and procedures governing corporate conduct and risk management; comprehensive business planning; effective segregation of duties; delegation of authority and personal accountability; careful selection and training of personnel; and sound and conservative accounting policies, which we regularly update. This structure ensures appropriate internal control over transactions, assets and records. We also regularly audit internal controls. These controls and audits are designed to provide us with reasonable assurance that the financial records are reliable for preparing financial statements and other financial information, assets are safeguarded against unauthorized use or disposition, liabilities are recognized, and we are in compliance with all regulatory requirements.

We, as OPG's Chief Executive Officer and Chief Financial Officer, will certify OPG's annual disclosure document filed with the OSC, which includes attesting to the effectiveness of OPG's disclosure controls and procedures, as required by Multilateral Instrument 52-109.

The Board of Directors, based on recommendations from its Audit and Risk Committee, reviews and approves the consolidated financial statements and the MD&A, and oversees management's responsibilities for the presentation and preparation of financial information, maintenance of appropriate internal controls, management and control of major risk areas and assessment of significant and related party transactions.

The consolidated financial statements have been audited by Ernst & Young LLP, independent external auditors appointed by the Board of Directors. The Auditors' Report outlines the auditors' responsibilities and the scope of their examination and their opinion on OPG's consolidated financial statements. The independent external auditors, as confirmed by the Audit and Risk Committee, had direct and full access to the Audit and Risk Committee, with and without the presence of management, to discuss their audit and their findings therefrom, as to the integrity of OPG's financial reporting and the effectiveness of the system of internal controls.

Jim Hankinson (signed)
President and Chief Executive Officer

Donn W. J. Hanbidge (signed)
Chief Financial Officer

February 7, 2006

AUDITORS' REPORT

To the Shareholder of Ontario Power Generation Inc.

We have audited the consolidated balance sheets of Ontario Power Generation Inc. as at December 31, 2005 and 2004 and the consolidated statements of income, retained earnings (deficit) and cash flows for the years then ended. These consolidated financial statements are the responsibility of Ontario Power Generation Inc.'s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of Ontario Power Generation Inc. as at December 31, 2005 and 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

ERNST & YOUNG LLP (SIGNED)
Chartered Accountants
Toronto, Canada
February 7, 2006

CONSOLIDATED STATEMENTS OF INCOME

Years Ended December 31

(millions of dollars except where noted)

	2005	2004
Revenue		
Revenue before Market Power Mitigation Agreement and revenue limit rebates	6,949	6,072
Market Power Mitigation Agreement rebate (note 17)	(412)	(1,154)
Revenue limit rebate (note 18)	(739)	-
	<u>5,798</u>	<u>4,918</u>
Fuel expense	1,297	1,153
Gross margin	<u>4,501</u>	<u>3,765</u>
Expenses		
Operations, maintenance and administration	2,516	2,594
Depreciation and amortization (note 5)	753	765
Accretion on fixed asset removal and nuclear waste management liabilities	476	453
Earnings on nuclear fixed asset removal and nuclear waste management funds	(381)	(313)
Property and capital taxes	107	103
Restructuring	10	20
	<u>3,481</u>	<u>3,622</u>
Income before the following:	1,020	143
Impairment of long-lived assets (note 5)	265	-
Other income	-	(8)
Income before interest, income taxes and extraordinary item	<u>755</u>	<u>151</u>
Net interest expense	197	189
Income (loss) before income taxes and extraordinary item	<u>558</u>	<u>(38)</u>
Income tax expense (recovery)		
Current	80	21
Future (note 10)	38	(101)
	<u>118</u>	<u>(80)</u>
Income before extraordinary item	440	42
Extraordinary item (note 10)	<u>74</u>	<u>-</u>
Net income	<u>366</u>	<u>42</u>
Basic and diluted income per common share before extraordinary item (dollars)	1.72	0.16
Basic and diluted income per common share (dollars)	<u>1.43</u>	<u>0.16</u>
Common shares outstanding (millions)	<u>256.3</u>	<u>256.3</u>

See accompanying notes to the consolidated financial statements

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS (DEFICIT)

As at December 31
(millions of dollars)

	2005	2004
Deficit, beginning of year	(105)	(147)
Net income	366	42
Retained earnings (deficit), end of year	261	(105)

See accompanying notes to the consolidated financial statements

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended December 31

(millions of dollars)

	2005	2004
Operating activities		
Net income	366	42
Adjust for non-cash items:		
Depreciation and amortization	753	765
Accretion on fixed asset removal and nuclear waste management liabilities	476	453
Earnings on nuclear fixed asset removal and nuclear waste management funds	(381)	(313)
Pension cost	115	92
Other post employment benefits and supplementary pension plans	181	157
Future income taxes	38	(101)
Transition rate option contracts	(36)	(52)
Provision for restructuring	10	20
Mark-to-market adjustment on energy contracts	18	5
Provision for used nuclear fuel	28	28
Impairment of long-lived assets	265	-
Excess inventory write-off	57	-
Extraordinary item	74	-
Regulatory assets and liabilities	7	-
Other	22	26
	1,993	1,122
Contributions to nuclear fixed asset removal and nuclear waste management funds	(454)	(454)
Expenditures on fixed asset removal and nuclear waste management	(90)	(71)
Reimbursement of expenditures on nuclear fixed asset removal and nuclear waste management	23	19
Contributions to pension fund	(254)	(154)
Expenditures on other post employment benefits and supplementary pension plans	(65)	(60)
Expenditures on restructuring (note 15)	(18)	(51)
Net changes to other long-term assets and liabilities	(87)	(26)
Changes in non-cash working capital balances (note 25)	153	(99)
Cash flow provided by operating activities	1,201	226
Investing activities		
Investment in regulatory assets (note 6)	(265)	-
Investment in fixed assets	(498)	(561)
Proceeds on sale of other fixed assets	3	18
Cash flow used in investing activities	(760)	(543)
Financing activities		
Issuance of long-term debt (note 8)	495	13
Repayment of long-term debt (note 8)	(4)	(6)
Net increase (decrease) in short-term notes (note 7)	(26)	26
Cash flow provided by financing activities	465	33
Net increase (decrease) in cash and cash equivalents	906	(284)
Cash and cash equivalents, beginning of year	2	286
Cash and cash equivalents, end of year	908	2

See accompanying notes to the consolidated financial statements

CONSOLIDATED BALANCE SHEETS

As at December 31

(millions of dollars)

	2005	2004
Assets		
Current assets		
Cash and cash equivalents	908	2
Accounts receivable (note 4)	538	346
Future income taxes (note 10)	18	44
Fuel inventory	581	569
Materials and supplies	115	92
	2,160	1,053
Fixed assets (note 5)		
Property, plant and equipment	15,172	15,114
Less: accumulated depreciation	3,760	3,174
	11,412	11,940
Other long-term assets		
Deferred pension asset (note 11)	663	524
Nuclear fixed asset removal and nuclear waste management funds (note 9)	6,788	5,976
Long-term materials and supplies	273	281
Regulatory assets (note 6)	266	-
Long-term accounts receivable and other assets	61	56
	8,051	6,837
	21,623	19,830

See accompanying notes to the consolidated financial statements

CONSOLIDATED BALANCE SHEETS

As at December 31

(millions of dollars)

	2005	2004
Liabilities		
Current liabilities		
Accounts payable and accrued charges (notes 15 and 16)	958	949
Market Power Mitigation Agreement rebate payable (note 17)	-	439
Revenue limit rebate payable (note 18)	739	-
Short-term notes payable (note 7)	-	26
Long-term debt due within one year (note 8)	806	5
Deferred revenue due within one year	12	12
Income and capital taxes payable (note 10)	81	12
	<u>2,596</u>	<u>1,443</u>
Long-term debt (note 8)	3,089	3,399
Other long-term liabilities		
Fixed asset removal and nuclear waste management (note 9)	8,759	8,339
Other post employment benefits and supplementary pension plans (note 11)	1,212	1,105
Long-term accounts payable and accrued charges	183	212
Deferred revenue	144	156
Future income taxes (note 10)	241	155
Regulatory liabilities (note 6)	12	-
	<u>10,551</u>	<u>9,967</u>
Shareholder's equity		
Common shares	5,126	5,126
Retained earnings (deficit)	261	(105)
	<u>5,387</u>	<u>5,021</u>
	<u>21,623</u>	<u>19,830</u>

Commitments and Contingencies (notes 2, 5, 7, 8, 9, 10, 12 and 14)

See accompanying notes to the consolidated financial statements

On behalf of the Board of Directors:

Honourable Jake Epp (signed)
Chairman

M. George Lewis (signed)
Director

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

1. DESCRIPTION OF BUSINESS

Ontario Power Generation Inc. was incorporated on December 1, 1998 pursuant to *the Business Corporations Act* (Ontario). As part of the reorganization of Ontario Hydro, under the *Electricity Act, 1998* and the related restructuring of the electricity industry in Ontario, Ontario Power Generation Inc. and its subsidiaries (collectively "OPG" or the "Company") purchased and assumed certain assets, liabilities, employees, rights and obligations of the electricity generation business of Ontario Hydro on April 1, 1999 and commenced operations on that date. Ontario Hydro has continued as Ontario Electricity Financial Corporation ("OEFEC"), responsible for managing and retiring Ontario Hydro's outstanding debt and other obligations.

2. BASIS OF PRESENTATION

These consolidated financial statements were prepared in accordance with Canadian generally accepted accounting principles. The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires Management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

The consolidated financial statements include the accounts of OPG and its subsidiaries. OPG accounts for its interests in jointly controlled entities using the proportionate consolidation method. All significant intercompany transactions have been eliminated on consolidation.

Certain of the 2004 comparative amounts have been reclassified from financial statements previously presented to conform to the 2005 financial statement presentation.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Cash and Cash Equivalents and Short-Term Investments

Cash and cash equivalents include cash on deposit and money market securities with a maturity of less than 90 days on the date of purchase. All other money market securities with a maturity on the date of purchase that is greater than 90 days, but less than one year, are recorded as short-term investments. These securities are valued at the lower of cost or market.

Interest earned on cash and cash equivalents and short-term investments of \$13 million (2004 – \$5 million) at an average effective rate of 2.8 per cent (2004 – 2.2 per cent) is offset against interest expense in the consolidated statements of income.

Sales of Accounts Receivable

Asset securitization involves selling assets such as accounts receivable to independent entities or trusts, which buy the receivables and then issue interests in them to investors. These transactions are accounted for as sales, given that control has been surrendered over these assets in return for net cash consideration. For each transfer, the excess of the carrying value of the receivables transferred over the estimated fair value of the proceeds received is reflected as a loss on the date of the transfer, and is included in net interest expense. The carrying value of the interests transferred is allocated to accounts receivable sold or interests retained according to their relative fair values on the day the transfer is made.

Fair value is determined based on the present value of future cash flows. Cash flows are projected using OPG's best estimates of key assumptions, such as discount rates, weighted average life of accounts receivable and credit loss ratios.

As part of the sales of accounts receivable, certain financial assets are retained and consist of interests in the receivables transferred. Any retained interests held in the receivables are accounted for at cost. The receivables are transferred on a fully serviced basis and do not create a servicing asset or liability.

Inventories

Fuel inventory is valued at weighted average cost.

Materials and supplies are valued at the lower of average cost or net realizable value with the exception of critical replacement parts which are unique to nuclear and fossil-fuelled generating stations. The cost of the critical replacement parts inventory is charged to operations on a straight-line basis over the remaining life of the related facilities and is classified in long-term assets.

Fixed Assets and Depreciation

Property, plant and equipment are recorded at cost. Interest costs incurred during construction are capitalized as part of the cost of the asset based on the interest rate on OPG's long-term debt. Expenditures for replacements of major components are capitalized.

Depreciation rates for the various classes of assets are based on their estimated service lives. Any asset removal costs that have not been specifically provided for in current or previous periods are also charged to depreciation expense. Repairs and maintenance are expensed when incurred.

Fixed assets are depreciated on a straight-line basis except for computers, and transport and work equipment, which are depreciated on a declining balance basis as noted below:

Darlington and Pickering B nuclear generating stations	25 years
Pickering A nuclear generating station	42 to 44 years ¹
Fossil generating stations	40 to 50 years ²
Hydroelectric generating stations	100 years
Administration and service facilities	50 years
Computers, and transport and work equipment assets – declining balance	9% to 40% per year
Major application software	5 years

¹ Units 1 and 4 of the Pickering A station are depreciated over a longer operating life as a result of the completion, during the 1980s, of the retubing of the Pickering A station and the refurbishment of Units 1 and 4, completed in 2005 and 2003 respectively.

² Commencing January 1, 2004, the coal-fired generating stations will be depreciated over the period from 2004 to 2007, due to the expected shutdown of these stations by the end of 2007, with the exception of the Nanticoke generating station which will be depreciated over the period to 2008.

Impairment of Fixed Assets

OPG evaluates its property, plant and equipment for impairment whenever conditions indicate that estimated undiscounted future net cash flows may be less than the net carrying amount of assets. In cases where the undiscounted expected future cash flows are less than the carrying amount, an impairment loss is recognized equal to the amount by which the carrying amount exceeds the fair value. Fair value is determined using expected discounted cash flows when quoted market prices are not available.

Long-Term Portfolio Investments

Long-term portfolio investments, other than investments owned by the Company's wholly owned subsidiary OPG Ventures Inc. ("OPGV"), are stated at amortized cost and include the nuclear fixed asset removal and nuclear waste management funds. Gains and losses on long-term investments are

recognized in other income when investments are sold. When a decline in the value of investments occurs, which is considered to be other than temporary, a provision for loss is established.

Investments owned by OPGV are recorded at fair value, and changes to the fair value of the investments are included in revenue in the period in which the change occurs. The fair values of these investments are estimated based on readily available market information or using estimation techniques based on historical performance.

Fixed Asset Removal and Nuclear Waste Management Liability

OPG recognizes asset retirement obligations for fixed asset removal and nuclear waste management, discounted for the time value of money. OPG has estimated both the amount and timing of future cash expenditures based on current plans for fixed asset removal and nuclear waste management. The liabilities are initially recorded at their estimated fair value, which is based on a discounted value of the expected costs to be paid.

On an ongoing basis, the liability is increased by the present value of the variable cost portion of the nuclear waste generated each year, with the corresponding amounts charged to operating expenses. Expenses relating to low and intermediate level waste are charged to depreciation and amortization expense. Expenses relating to the disposal of nuclear used fuel are charged to fuel expense. The liability may also be adjusted due to any changes in the estimated amount or timing of the underlying future cash flows. Upon settlement of the liability, a gain or loss would be recorded.

Accretion arises because liabilities for fixed asset removal and nuclear waste management are reported on a net present value basis. Accretion expense is the increase in the carrying amount of the liabilities due to the passage of time. The resulting expense is included in operating expenses.

The asset retirement cost is capitalized by increasing the carrying value of the related fixed assets. The capitalized cost is depreciated over the remaining useful life of the related fixed assets and is included in depreciation expense.

Nuclear Fixed Asset Removal and Nuclear Waste Management Funds

Pursuant to the Ontario Nuclear Funds Agreement (“ONFA”) between OPG and the Province of Ontario, OPG established the Used Fuel Fund and a Decommissioning Fund (together the “Nuclear Funds”). The Used Fuel Fund is intended to fund expenditures associated with the disposal of highly radioactive used nuclear fuel bundles, while the Decommissioning Fund was established to fund expenditures associated with nuclear fixed asset removal and the disposal of low and intermediate level nuclear waste materials. OPG maintains the Nuclear Funds in third party custodial accounts that are segregated from the rest of OPG’s assets.

The Nuclear Funds are invested in fixed income and equity securities, which OPG records as long-term investments and accounts for at their amortized cost value. Therefore, gains and losses are recognized only upon the sale of an underlying security. As such, there may be unrealized gains and losses associated with the investments in the Nuclear Funds, which OPG has not recognized in its consolidated financial statements.

Revenue Recognition

All of OPG’s electricity generation is sold into the real-time energy spot market administered by the Independent Electricity System Operator (“IESO”). Prior to April 1, 2005, revenue was recorded as electricity was generated and metered based on the spot market sales price, net of the Market Power Mitigation Agreement rebate and hedging activities. At each balance sheet date, OPG computed the average spot energy price that prevailed since the beginning of the current settlement period and recognized a Market Power Mitigation Agreement rebate if the average price exceeded 3.8¢/kilowatt-hour (“kWh”), based on the amount of energy subject to the rebate.

Effective April 1, 2005, the generation from most of OPG's baseload hydroelectric facilities and all of its nuclear facilities became rate regulated. OPG continues to receive the spot market price for the output from its remaining hydroelectric, fossil-fuelled and wind generating stations, subject to a revenue limit. As a result, energy revenue generated from the nuclear facilities is recognized based on a regulated price of 4.95¢/kWh. The regulated price received by OPG for the first 1,900 megawatt hours (MWh) of production from the regulated hydroelectric facilities in any hour is 3.3¢/kWh. Any production from these regulated hydroelectric facilities above 1,900 MWh in any hour receives the Ontario electricity spot market price. The production from OPG's other generating assets remains unregulated and continues to be sold at the Ontario electricity spot market price. However, 85 per cent of the generation output from OPG's other generating assets, excluding the Lennox generating station, Transition – Generation Corporation Designated Rate Options ("TRO") volumes and forward sales as of January 1, 2005, are subject to a revenue limit based on an average price of 4.7¢/kWh. This revenue limit was originally established for a period of 13 months ending April 30, 2006.

OPG also sells into, and purchases from, interconnected markets of other provinces and the U.S. northeast and midwest. All contracts that are not designated as hedges are recorded in the consolidated balance sheets at market value with gains or losses recorded in the consolidated statements of income. Gains and losses on energy trading contracts (including those to be physically settled) are recorded on a net basis in the consolidated statements of income. Accordingly, power purchases of \$228 million in 2005 and \$170 million in 2004 were netted against revenue.

OPG derives non-energy revenue under the terms of a lease arrangement with Bruce Power L.P. ("Bruce Power") related to the Bruce nuclear generating stations. This includes lease revenues, interest income and revenues for engineering analysis and design, technical and ancillary services. OPG also earns revenue from its joint venture share of the Brighton Beach Power Limited Partnership ("Brighton Beach") related to an energy conversion agreement between Brighton Beach and Coral Energy Canada Inc. ("Coral"). In addition, non-energy revenue includes isotope sales to the medical industry and real estate rentals. Revenues from these activities are recognized as services are provided or products are delivered.

Foreign Currency Translation

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian currency at year-end exchange rates. Any resulting gain or loss is reflected in other revenue.

Derivatives

OPG is exposed to changes in electricity prices associated with a wholesale spot market for electricity in Ontario. To hedge the commodity price risk exposure associated with changes in the wholesale price of electricity, OPG enters into various energy and related sales contracts. These contracts are expected to be effective as hedges of the commodity price exposure on OPG's generation portfolio. Gains or losses on hedging instruments are recognized in income over the term of the contract when the underlying hedged transactions occur. These gains or losses are included in unregulated revenue and are not recorded on the consolidated balance sheets. All contracts not designated as hedges are recorded as assets or liabilities at fair value with changes in fair value recorded in other revenue.

OPG also enters into derivative contracts with major financial institutions to manage the Company's exposure to foreign currency movements. Foreign exchange translation gains and losses on these foreign currency denominated derivative contracts are recognized as an adjustment to the purchase price of the commodity or goods received.

OPG is exposed to changes in market interest rates on debt expected to be issued in the future. OPG uses interest rate derivative contracts to hedge this exposure. Gains and losses on interest rate hedges are recorded as an adjustment to interest expense for the debt being hedged. Gains and losses that do not meet the effectiveness criteria are recorded through net income in the period incurred.

OPG utilizes emission reduction credits ("ERCs") and allowances to manage emissions within the prescribed regulatory limits. ERCs are purchased from trading partners in Canada and the United States.

Emission allowances are obtained from the Province and purchased from trading partners in Ontario. The cost of ERCs and allowances are held in inventory and charged to OPG's operations at average cost as part of fuel expense as required. Options to purchase ERCs are accounted for as derivatives and are recorded at estimated market value.

Hedge accounting is applied when the derivative instrument is designated as a hedge and is expected to be effective throughout the life of the hedged item. When such derivative instrument ceases to exist or be effective as a hedge, or when designation of a hedging relationship is terminated, any associated deferred gains or losses are carried forward to be recognized in income in the same period as the corresponding gains or losses associated with the hedged item. When a hedged item ceases to exist, any associated deferred gains or losses are recognized in the current period's consolidated statement of income.

Research and Development

Research and development costs are charged to operations in the year incurred. Research and development costs incurred to discharge long-term obligations such as the nuclear waste management liabilities, for which specific provisions have already been made, are charged to the related liability.

Pension and Other Post Employment Benefits

OPG's post employment benefit programs include a contributory defined benefit registered pension plan, a defined benefit supplementary pension plan, group life insurance, health care and long-term disability benefits. OPG accrues its obligations under pension and other post employment benefit ("OPEB") plans. The obligations for pension and other post retirement benefit costs are determined using the projected benefit method pro-rated on service. The obligation for long-term disability benefits is determined using the projected benefit method on a terminal basis. The obligations are affected by salary levels, inflation, and cost escalation. Pension and OPEB costs and obligations are determined annually by independent actuaries using management's best estimate assumptions. The discount rates used by OPG in determining projected benefit obligations and the costs for the Company's employee benefit plans are based on representative AA corporate bond yields.

Pension fund assets are valued using market-related values for purposes of determining actuarial gains or losses and the expected return on plan assets. The market-related value recognizes gains and losses on equity assets relative to a six per cent assumed real return over a five-year period.

Pension and OPEB costs include current service costs, interest costs on the obligations, the expected return on pension plan assets, adjustments for plan amendments and adjustments for actuarial gains or losses, which result from changes in assumptions and experience gains and losses. Past service costs arising from pension and OPEB plan amendments are amortized on a straight-line basis over the expected average remaining service life of the employees covered by the plan, since OPG will realize the economic benefit over that period. Due to the long-term nature of post-employment liabilities, the excess of the net cumulative unamortized gain or loss, over 10 per cent of the greater of the benefit obligation and the market-related value of the plan assets, is also amortized over the expected average remaining service life.

When the recognition of the transfer of employees and employee-related benefits gives rise to both a curtailment and a settlement, the curtailment is accounted for prior to the settlement. A curtailment is the loss by employees of the right to earn future benefits under the plan. A settlement is the discharge of a plan's liability.

Taxes

Under the *Electricity Act, 1998*, OPG is responsible for making payments in lieu of corporate income and capital taxes to the OEFC. These payments are calculated in accordance with the *Income Tax Act* (Canada) and the *Corporations Tax Act* (Ontario), and are modified by the *Electricity Act, 1998* and related regulations. This effectively results in OPG paying taxes similar to what would be imposed under the federal and Ontario tax acts.

OPG uses the liability method of accounting for income taxes for the unregulated segments of its business. Under the liability method, income taxes are recognized as a result of temporary differences arising from the difference between the tax basis of an asset or liability and its carrying value in the balance sheet, the carry-forward of unused tax losses and income tax reductions. Future income tax assets and liabilities are measured using income tax rates expected to apply in the years in which temporary differences are expected to reverse. The effect on future income tax assets and liabilities of a change in tax rates is included in income in the period the change is substantively enacted. Future income tax assets are evaluated and if realization is not considered 'more likely than not', a valuation allowance is established.

Commencing April 1, 2005, with the introduction of rate regulation, OPG accounts for income taxes related to the rate regulated segments of its business using the taxes payable method. Under the taxes payable method, OPG does not recognize future income taxes related to the rate regulated segments of its business to the extent that these future income taxes are expected to be recovered in the regulated rates charged to future customers.

OPG makes payments in lieu of property tax on its nuclear and fossil-fuelled generating assets to the OEFC, and also pays property taxes to municipalities.

OPG pays charges on gross revenue derived from the annual generation of electricity from its hydroelectric generating assets. The gross revenue charge ("GRC") includes a fixed percentage charge applied to the annual hydroelectric generation derived from stations located on provincial Crown lands, in addition to graduated rate charges applicable to all hydroelectric stations. GRC costs are included in fuel expense.

Business Segments

As noted in Note 19, OPG changed its definition of business segments on April 1, 2005 from Generation and Energy Marketing to Regulated – Nuclear, Regulated – Hydroelectric and Unregulated Generation. OPG will continue to report other activities, including trading activities, which were previously reported separately, in the Other category. As a result of this change in definition, OPG has reclassified the comparative periods to be consistent with the current presentation of business segments.

Changes in Accounting Policies

Rate Regulated Accounting

In December 2004, the *Electricity Restructuring Act, 2004* (Bill 100) received Royal Assent. A regulation made pursuant to that statute in February 2005 provides that OPG receive regulated prices beginning April 1, 2005, for its baseload hydroelectric and nuclear facilities. This includes electricity generated by Sir Adam Beck 1, 2 and Pump generating station, DeCew Falls 1 and 2, and R.H. Saunders hydroelectric facilities, and Pickering A and B, and Darlington nuclear generating stations.

OPG's regulated prices were determined by the Province based on total projected production and costs of operation, plus the cost of capital including an average five per cent return on equity. The initial prices took effect April 1, 2005, and are expected to remain in effect until at least March 31, 2008, at which time it is anticipated that the Ontario Energy Board ("OEB") will establish new regulated prices. If there are changes to the fundamental assumptions on which these regulated prices were developed, the Province may amend these initial prices.

The OEB is a self-funding Crown corporation. Its mandate and authority come from the *Ontario Energy Board Act, 1998*, the *Electricity Act, 1998*, and a number of other provincial statutes. The OEB is an independent, quasi-judicial tribunal that reports to the Legislature of the Province through the Minister of Energy. It regulates all market participants in the province's natural gas and electricity industries and carries out its regulatory functions through public hearings and other more informal processes such as consultations.

Accounting standards recognize that rate regulation can create economic benefits and obligations, which are reported in the consolidated financial statements as regulatory assets and liabilities. When the regulation provides assurance that incurred costs will be recovered in the future, then OPG may defer those costs and report them as a regulatory asset. If current recovery is provided for costs expected to be incurred in the future, then OPG reports a regulatory liability. Also, if the regulation provides for lesser or greater than planned revenue to be received or returned by OPG through future rates, then OPG recognizes and reports a regulatory asset or liability, respectively. The measurement of such regulatory assets and liabilities are subject to certain estimates and assumptions, including assumptions made in the interpretation of the regulation.

Income Taxes

Commencing April 1, 2005, with the introduction of rate regulation, OPG accounts for income taxes related to the rate regulated segments of its business using the taxes payable method.

New Accounting Recommendations

Consolidation of Variable Interest Entities

In September 2004, the CICA amended Accounting Guideline 15, *Consolidation of Variable Interest Entities*, originally issued in June 2003, to harmonize with the revised Financial Accounting Standards Board Interpretation No. 46, *Consolidation of Variable Interest Entities* ("FIN 46R"). The new guideline requires the consolidation of variable interest entities ("VIEs") by the primary beneficiary. A VIE is an entity where (i) its equity investment at risk is insufficient to permit the entity to finance its activities without additional subordinated support from others and/or where certain essential characteristics of a controlling financial interest are not met, and (ii) it does not meet specified exemption criteria. The primary beneficiary is the enterprise that will absorb or receive the majority of the VIEs' expected losses, expected residual returns, or both.

OPG is involved with various joint venture and other arrangements and has sold trade receivables under an asset securitization arrangement. OPG concluded that the joint venture and other arrangements with which it is involved are not VIEs, and that it is not the primary beneficiary of, nor does it have a significant variable interest in, the trust to which it sold trade receivables.

Investment Companies

In January 2004, the CICA issued Accounting Guideline 18, *Investment Companies* ("AcG-18"). The new guideline requires investments owned by entities that meet the investment companies criteria, to be recorded at fair value with gains and losses recognized in net income. During 2005, OPG applied the new guideline to investments that it owns.

Future Accounting Policy Changes

In 2005, the CICA issued three new accounting standards: Handbook Section 1530, Comprehensive Income, Handbook Section 3855, Financial Instruments – Recognition and Measurement, and Handbook Section 3865, Hedges. These standards apply to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2006.

These standards will be effective for OPG beginning in 2007. The impact of implementing these new standards on OPG's consolidated financial statements is not yet determinable as it will be dependent on outstanding positions and their fair values at the time of transition. The following provides further information on each of the three new accounting standards as they relate to OPG.

Comprehensive Income

As a result of adopting these standards, a new category, accumulated other comprehensive income, will be added to shareholder's equity on the consolidated balance sheets. Major components for this category will include unrealized gains and losses on financial assets classified as available-for-sale, unrealized foreign currency translation amounts, net of hedging, and changes in the fair value of the effective portion of cash flow hedging instruments. These amounts will be recorded in the statement of other comprehensive income until the criteria for recognition in the consolidated statement of income are met.

Financial Instruments – Recognition and Measurement

Under the new standard, for accounting purposes, financial assets will be classified as one of the following: held-to-maturity, loans and receivables, held-for-trading or available-for-sale, and financial liabilities will be classified as held-for-trading or other than held-for-trading. Financial assets and liabilities held-for-trading will be measured at fair value with gains and losses recognized in net income. Financial assets held-to-maturity, loans and receivables and financial liabilities other than those held-for-trading, will be measured at amortized cost. Available-for-sale instruments will be measured at fair value with unrealized gains and losses recognized in other comprehensive income. The standard also permits designation of any financial instrument as held-for-trading upon initial recognition. All derivatives, including embedded derivatives that must be separately accounted for, generally must be classified as held for trading and recorded at fair value in the consolidated balance sheets.

Hedges

This new standard specifies the criteria under which hedge accounting can be applied and how hedge accounting is to be executed for each of the permitted hedging strategies: fair value hedges, cash flow hedges and hedges of a foreign currency exposure of a net investment in a self-sustaining foreign operation. In a fair value hedging relationship, the carrying value of the hedged item is adjusted by gains or losses attributable to the hedged risk and recognized in net income. This change in fair value of the hedged item, to the extent that the hedging relationship is effective, is offset by changes in the fair value of the derivative. In a cash flow hedging relationship, the effective portion of the change in the fair value of the hedging derivative will be recognized in other comprehensive income. The ineffective portion will be recognized in net income. The amounts recognized in accumulated other comprehensive income will be reclassified to net income in the periods in which net income is affected by the variability in the cash flows of the hedged item. In hedging a foreign currency exposure of a net investment in a self-sustaining foreign operation, foreign exchange gains and losses on the hedging instruments will be recognized in other comprehensive income.

4. SALE OF ACCOUNTS RECEIVABLE

On October 1, 2003, the Company signed an agreement to sell an undivided co-ownership interest in its current and future accounts receivable (the "receivables") to an independent trust. The Company also retains an undivided co-ownership interest in the receivables sold to the trust. Under the agreement, OPG continues to service the receivables. The transfer provides the trust with ownership of a share of the payments generated by the receivables, computed on a monthly basis. The trust's recourse to the Company is generally limited to its income earned on the receivables. In December 2005, OPG extended the agreement to August 2009.

OPG reflected the initial transfer to the trust of the co-ownership interest, and subsequent transfers required by the revolving nature of the securitization, as sales in accordance with CICA Accounting Guideline 12, *Transfer of Receivables*. In accordance with this Guideline, the proceeds of each sale to the trust were deemed to be the cash received from the trust net of the undivided co-ownership interest retained by the Company. For 2005, the Company has recognized pre-tax charges of \$9 million (2004 – \$8 million) on such sales at an average cost of funds of 3.1 per cent (2004 – 2.6 per cent). As at December 31, 2005, OPG had sold receivables of \$300 million from its total portfolio of \$668 million.

The accounts receivable reported and securitized by the Company are as follows:

<i>(millions of dollars)</i>	Principal amount of receivables as at December 31		Average balance of receivables for year ended December 31	
	2005	2004	2005	2004
Total receivables portfolio ¹	668	490	559	470
Receivables sold	300	300	300	300
Receivables retained	368	190	259	170
Average cost of funds			3.1%	2.6%

¹ Amount represents receivables outstanding, including receivables that have been securitized, which the Company continues to service.

An immediate 10 per cent or 20 per cent adverse change in the discount rate would not have a material effect on the current fair value of the retained interest. There were no credit losses for the year ended December 31, 2005 and 2004.

Details of cash flows from securitizations for the years ended December 31 are as follows:

<i>(millions of dollars)</i>	2005	2004
Collections reinvested in revolving sales ¹	3,600	3,600
Cash flows from retained interest	3,104	2,043

¹ Given the revolving nature of the securitization, the cash collections received on the receivables securitized are immediately reinvested in additional receivables resulting in no further cash proceeds to the Company over and above the initial cash amount of \$300 million. The amounts reflect the cumulative of 12 monthly amounts.

5. FIXED ASSETS

Depreciation and amortization expense consists of the following:

<i>(millions of dollars)</i>	2005	2004
Depreciation and amortization	748	758
Nuclear waste management costs	5	7
	753	765

Fixed assets consist of the following:

<i>(millions of dollars)</i>	2005	2004
Property, plant and equipment		
Nuclear generating stations	4,754	4,326
Regulated Hydroelectric generating stations	4,379	4,345
Unregulated Hydroelectric generating stations	3,447	3,432
Fossil-fuelled generating stations	1,411	1,596
Other fixed assets	833	850
Construction in progress	348	565
	15,172	15,114
Less: accumulated depreciation		
Generating stations	3,497	2,935
Other fixed assets	263	239
	3,760	3,174
	11,412	11,940

The asset under capital lease was \$203 million in 2004 and was included in other fixed assets. There were no assets under capital lease as at December 31, 2005. Accumulated depreciation on the leased asset at December 31, 2004 was \$53 million. Interest capitalized at six per cent during the years ended December 31, 2005 and 2004 was \$27 million and \$30 million, respectively.

Impairment of Long-Lived Assets

The accounting estimates related to asset impairment require significant management judgment to identify factors such as short and long-term forecasts for future sales prices, the supply of electricity in Ontario, inflation, fuel prices and station lives. The amount of the future cash flow that OPG will ultimately realize with respect to these assets could differ materially from the carrying values recorded in the consolidated financial statements.

Pickering A Nuclear Generating Station Units 2 and 3

OPG completed an assessment of the cost, schedule and risks related to the return to service of Units 2 and 3 at the Pickering A nuclear generating station. This included an assessment of the ability of these units to perform at an acceptable capability factor over the remaining 12 to 20 years of operations. This assessment incorporated recent findings from inspection programs with respect to feeder pipe and steam generator degradation mechanisms, and potential degradation of the calandria vault components, all of which could impact the future capability factor, operating costs and the life of the units. Upon consideration of the scope of the refurbishment work, the costs and the risks related to the return to service of these two units, and the Company's focus on improving the performance of its other nuclear units, OPG's Board of Directors decided that while technically feasible, the return to service of these units was not justified on a commercial basis. Accordingly, OPG recorded an impairment loss of \$63 million in the second quarter of 2005 related to the carrying amount of these two units including construction in progress. In addition to the impairment loss for these two units, OPG recorded OM&A expenses of \$57 million related to the write-off of inventory identified as excess or unusable, as a result of not returning Units 2 and 3 to service.

OPG expects to recover the amounts recorded in the deferral account relating to non-capital costs incurred after January 1, 2005 associated with the return to service of Units 2 and 3. As at December 31, 2005, the deferral account relating to Units 2 and 3 was \$19 million.

As a result of the decision not to proceed with the return to service of these two units, OPG continues to assess the need to provide for any additional costs, including the cost associated with preparing the units for safe storage, any impacts on cost estimates for asset retirement obligation and any other additional exit costs. Such charges may have a significant impact on operating results in future periods.

Lennox Generating Station

As a result of the Government's "Request for Information/Request for Proposal for 2,500 MW of New Clean Generation and Demand Side Management Projects" released in September 2004 and the related contractual arrangements, future wholesale electricity market revenue is expected to be lower than previously anticipated. As a relatively high variable cost plant, the Lennox generating station will not be able to recover its fixed operating costs and its carrying value from the wholesale electricity market in the future. Given these factors, OPG had initiated discussions with the Province, with the expectation of entering into a contractual arrangement for the recovery of the annual fixed operating costs and the carrying value of the Lennox generating station. In March 2005, OPG was advised by the Province that it would continue to support OPG in negotiating an arrangement that would allow for the recovery of fixed operating costs, but that the Province would not support an arrangement that would allow for the recovery of the carrying value of the Lennox generating station. As a result of this change in circumstance, OPG recorded the impairment loss of \$202 million in the first quarter of 2005. OPG has since negotiated a contract with the Independent Electricity System Operator ("IESO"), pursuant to the market rules, to recover its operating costs for a one-year period ending September 30, 2006. The contract with the IESO has been submitted to the OEB for approval.

6. REGULATORY ASSETS AND LIABILITIES

OPG recorded the following regulatory assets and liabilities as at December 31, 2005:

<i>(millions of dollars)</i>	2005
Regulatory assets	
Pickering A return to service costs deferral account	261
Ancillary services revenue variance account	5
Total regulatory assets	266
Regulatory liabilities	
Hydroelectric production variance account	4
Other	8
Total regulatory liabilities	12

Pickering A Return to Service Costs

Effective January 1, 2005, in accordance with regulations pursuant to the *Electricity Restructuring Act, 2004*, OPG is required to establish a deferral account in connection with non-capital costs that are associated with the return to service of units at the Pickering A nuclear generating station. As a result, the change in accounting was prospectively adopted on January 1, 2005, with no retroactive adoption. As at December 31, 2005, the deferral account was \$261 million, consisting of non-capital costs, net of amortization, of \$228 million relating to Unit 1, \$19 million relating to Units 2 and 3, \$11 million of general return to service costs, and interest of \$7 million accreted at the average cost of debt of six per cent. Upon OPG becoming subject to regulated prices established by the OEB, expected after March 31, 2008, the OEB is directed by the regulation to ensure that OPG recovers any balance in the deferral account on a straight-line basis over a period not to exceed 15 years.

In November 2005, as a result of the return to commercial service of Unit 1 at the Pickering A nuclear generating station, OPG commenced amortization of the Pickering A return to service regulatory asset to OM&A expenses. The basis for amortization is consistent with that reflected in interim regulated rates and resulted in OPG recording \$4 million in OM&A expenses as at December 31, 2005.

Had OPG not charged costs to the deferral account as required by the regulations, an additional \$254 million would have been charged to OM&A expense and \$7 million to net interest expense during 2005.

Variance Accounts

Effective April 1, 2005, in accordance with the regulations pursuant to the *Electricity Restructuring Act, 2004*, OPG was directed to establish variance accounts for costs incurred on or after April 1, 2005 that are associated with differences in hydroelectric electricity production due to differences between forecast and actual water conditions, changes in nuclear electricity production due to unforeseen changes to the law or to unforeseen technological changes, changes to revenues assumed for ancillary revenues from the regulated facilities, acts of God (including severe weather events), and transmission outages and transmission restrictions. OPG recorded an asset as at December 31, 2005 of \$5 million, reflecting ancillary services revenue that was unfavourable compared to that forecasted for 2005. OPG recorded a liability as at December 31, 2005 of \$4 million, reflecting water conditions that were favourable compared to those forecasted for 2005. Upon OPG becoming subject to regulated prices established by the OEB, the OEB is directed by the regulation to ensure recovery to the extent that the OEB is satisfied that the costs recorded in the account were prudently incurred and accurately recorded. Any balances approved by the OEB will be amortized over a period not to exceed three years.

Had OPG not accounted for the variances as a regulatory asset and liability, revenue for 2005 would have been lower by \$1 million.

The other regulatory liability consists of a portion of non-regulated revenue earned by OPG's regulated assets, which will result in a reduction of future regulated rates to be established by the OEB.

7. SHORT-TERM CREDIT FACILITIES

OPG's current 364-day term \$1 billion revolving committed bank credit facility was renewed on May 24, 2005. The new facility is divided into two tranches – a \$500 million 364-day term tranche maturing May 23, 2006, and a \$500 million three-year term tranche maturing May 23, 2008. The total credit facility will continue to be used primarily as support for notes issued under OPG's commercial paper program. As at December 31, 2005, OPG had no borrowings outstanding under this commercial paper program (2004 – \$26 million). As at December 31, 2005 and 2004, OPG had no other outstanding borrowing under this facility.

OPG also maintains \$26 million (2004 – \$26 million) in short-term uncommitted overdraft facilities as well as \$215 million (2004 – \$200 million) of short-term uncommitted credit facilities, which support the issuance of Letters of Credit. OPG uses Letters of Credit to support supplementary pension plans and is required to post the Letters of Credit as collateral with Local Distribution Companies ("LDCs") as prescribed by the OEB's Retail Settlement Code. At December 31, 2005, there were approximately \$157 million (2004 – \$155 million) of Letters of Credit issued for the supplementary pension plans and collateral requirements to the LDCs.

8. LONG-TERM DEBT

Long-term debt consists of the following:

<i>(millions of dollars)</i>	2005	2004
Notes payable to the OEFC	3,695	3,200
Capital lease obligations	-	3
Share of non-recourse limited partnership debt	200	201
	3,895	3,404
Less: due within one year		
Notes payable to the OEFC	800	-
Capital lease obligations	-	3
Share of limited partnership debt	6	2
	806	5
Long-term debt	3,089	3,399

Holders of the senior debt are entitled to receive, in full, amounts owing in respect of the senior debt before holders of the subordinated debt are entitled to receive any payments. The OEFC currently holds all of OPG's outstanding senior and subordinated notes.

The maturity dates as at December 31, 2005 for notes payable to the OEFC are as follows:

Year of Maturity	Interest Rate (%)	Principal Outstanding (millions of dollars)		
		Senior Notes	Subordinated Notes	Total
2006	5.70%	800	-	800
2007	5.85%	400	-	400
2008	5.90%	400	-	400
2009	6.01%	350	-	350
2010	6.00%	595	375	970
2011	6.65%	-	375	375
2012	5.72%	400	-	400
		2,945	750	3,695

In December 2004, OPG reached an agreement with the OEFC to defer payment on the \$500 million principal amount of senior notes maturing in March and September 2005 by extending the maturity dates by five years. The interest rates remain unchanged. In March 2005, the Company reached an agreement with the OEFC to obtain additional financing up to \$600 million, which can be drawn until March 31, 2006. In April 2005, \$400 million was drawn under this facility, with a seven-year term.

The Company also reached an agreement with the OEFC to satisfy, through the issue of additional senior notes of \$95 million and \$98 million respectively, to mature in 2010, its \$95 million interest obligation due in March 2005 and the \$98 million interest obligation due in September 2005 related to the debt owing to the OEFC of \$3.2 billion. As a result of an improved liquidity position, OPG elected to pay the interest due in September 2005 and not issue the \$98 million note.

Interest paid in 2005 was \$235 million (2004 – \$218 million), of which \$220 million relates to interest paid on long-term debt (2004 – \$213 million).

In September 2005, OPG reached an agreement with the OEFC to provide debt financing for the Niagara tunnel project. The funding, which is up to \$1 billion over the duration of the project, will be in the form of 10-year notes, which will be issued quarterly to meet the project's obligations. Interest will be fixed for

each note issued at the time of advance at a rate equal to the prevailing Benchmark Government of Canada 10-Year Bond, plus a credit spread determined by the OEFC based on a survey of market rates.

In October 2005, OPG reached a similar agreement with the OEFC to finance the Thunder Bay Gas Conversion project. There will be up to \$95 million available to OPG under this credit facility, that will be drawn as needed over the projected two-year construction period. OPG is expected to make its first draw under this facility in the first quarter of 2006.

9. FIXED ASSET REMOVAL AND NUCLEAR WASTE MANAGEMENT

The liability for fixed asset removal and nuclear waste management on a present value basis consists of the following:

<i>(millions of dollars)</i>	2005	2004
Liability for nuclear used fuel management	4,940	4,693
Liability for nuclear decommissioning and low and intermediate level waste management	3,627	3,457
Liability for non-nuclear fixed asset removal	192	189
Fixed asset removal and nuclear waste management liability	8,759	8,339

The change in the fixed asset removal and nuclear waste management liability for the years ended December 31, 2005 and 2004, is as follows:

<i>(millions of dollars)</i>	2005	2004
Liability, beginning of year	8,339	7,921
Increase in liability due to accretion	476	453
Increase in liability due to nuclear used fuel and nuclear waste management variable expenses	34	35
Fixed asset removal of partnership interests	-	1
Liabilities settled by expenditures on waste management	(90)	(71)
Liability, end of year	8,759	8,339

OPG's asset retirement obligations are comprised of expected costs to be incurred up to and upon termination of operations and the closure of nuclear and fossil-fuelled generating plant facilities. Costs will be incurred for activities such as dismantling, demolition and disposal of facilities and equipment, remediation and restoration of sites and the ongoing and long-term management of nuclear used fuel and low and intermediate level waste material.

The following costs are recognized as a liability:

- The present value of the costs of dismantling the nuclear and fossil-fuelled production facilities at the end of their useful lives
- The present value of the fixed cost portion of any nuclear waste management programs that are required based on the total volume of waste expected to be generated over the assumed life of the stations
- The present value of the variable cost portion of any nuclear waste management program to take into account actual waste volumes incurred to date.

The determination of the accrual for fixed asset removal and nuclear waste management costs requires significant assumptions, since these programs run for many years. Plant closures are projected to occur between one and 14 years from today, depending on the plant. Current plans include cash flow estimates to 2057 for decommissioning nuclear stations and to approximately 2100 for nuclear used fuel management. The undiscounted amount of estimated cash flows associated with the liability expected to be incurred up to and upon closure of generating stations is approximately \$20 billion. The discount rate used to calculate the present value of the liabilities at December 31, 2005 was 5.75 per cent (2004 – 5.75 per cent) and the cost escalation rates ranged from two per cent to four per cent. Under the terms of the lease agreement with Bruce Power, OPG continues to be responsible for the nuclear fixed asset removal and nuclear waste management liabilities associated with the Bruce nuclear generating stations.

The significant assumptions underlying operational and technical factors used in the calculation of the accrued liabilities are subject to periodic review. The estimate of the liability is being updated in 2006. Changes to these assumptions, including changes to assumptions on the timing of the programs, financial indicators or the technology employed, could result in significant changes to the value of the accrued liabilities. With programs of this duration and the evolving technology to handle the nuclear waste, there is a significant degree of uncertainty surrounding the measurement accuracy of the costs for these programs, which may increase or decrease over time.

Liability for Nuclear Used Fuel Management Costs

The liability for nuclear used fuel management represents the cost of managing the highly radioactive used nuclear fuel bundles. The current assumptions that have been used to establish the accrued used fuel costs include long-term management of the spent fuel bundles through deep geological disposal; an in-service date of 2035 for used nuclear fuel disposal facilities; and an average transportation distance of 1,000 kilometres between nuclear generating facilities and the disposal facilities. Alternatives to deep geological disposal have been studied by Canadian nuclear utilities via the Nuclear Waste Management Organization as part of the options study required by the federal *Nuclear Fuel Waste Act* (Canada) (“NFWA”). The options study was submitted to the federal government in November 2005. The federal government will decide which management alternative should be followed. The pending decision could have a significant impact on OPG's estimate of the liability.

Liability for Nuclear Decommissioning and Low and Intermediate Level Waste Management Costs

The liability for nuclear decommissioning and low and intermediate level waste management represents the estimated costs of decommissioning nuclear generating stations after the end of their service lives, as well as the cost of managing low and intermediate level radioactive wastes generated by the nuclear stations. The significant assumptions used in estimating future nuclear fixed asset removal costs include decommissioning of nuclear generating stations on a deferred dismantlement basis where the reactors will remain in a safe storage state for a 30-year period prior to a 10-year dismantlement period. Current plans assume that low and intermediate level waste arising during decommissioning will be disposed of at the facilities developed for disposal of operational low and intermediate level waste.

The life cycle costs of low and intermediate level waste management include the costs of processing and storage of such radioactive wastes during and following the operation of the nuclear stations, as well as the costs of ultimate long-term disposal of these wastes. The current assumptions used to establish the accrued low and intermediate level waste management costs include: an in-service date of 2015 for disposal facilities for low level waste; co-locating short-lived intermediate level waste with low level waste starting in 2015; and co-locating long-lived intermediate level waste with used fuel starting in 2035. Plans are currently proceeding for development of a deep geologic repository at the Western Waste Management Facility. Agreements are in place with the Municipality of Kincardine for this repository.

Liability for Non-Nuclear Fixed Asset Removal Costs

The liability for non-nuclear fixed asset removal is based on third-party cost estimates after an in-depth review of active plant sites and an assessment of required clean-up and restoration activities. This liability represents the estimated costs of decommissioning fossil-fuelled generating stations at the end of their service lives. The estimated retirement date of these stations is between 2007 and 2034.

In addition to the \$95 million liability for active sites, OPG also has an asset retirement obligation liability of \$97 million for decommissioning and restoration costs associated with plant sites that have been divested or are no longer in use.

OPG has no legal obligation associated with the decommissioning of its hydroelectric generating facilities. Also, the costs cannot be reasonably estimated because of the long service life of these assets. With either maintenance efforts or rebuilding, the water control structures are assumed to be used for the foreseeable future. Accordingly, OPG has not recognized a liability for the decommissioning of its hydroelectric generating facilities.

Ontario Nuclear Funds Agreement

OPG sets aside funds to be used specifically for discharging its nuclear fixed asset removal and nuclear waste management liabilities. In July 2003, OPG and the Province completed arrangements, pursuant to the ONFA. To comply with the ONFA, OPG established the Nuclear Funds. OPG jointly oversees the investment management of the Nuclear Funds with the Province. The assets of the Nuclear Funds are maintained in third party custodian accounts that are segregated from the rest of OPG's assets.

The Decommissioning Fund will be used to fund the future costs of nuclear fixed asset removal and long-term low and intermediate level nuclear waste management and a portion of used fuel storage costs after station life. The initial funding of the Decommissioning Fund was intended to be sufficient to fully discharge the 1999 estimate of the liability. OPG bears the risk and liability for cost estimate increases and fund earnings in the Decommissioning Fund.

The Used Fuel Fund will be used to fund future costs of long-term nuclear used fuel waste management. OPG is responsible for the risk and liability for cost increases for used fuel waste management, subject to graduated liability thresholds specified in the ONFA, which limit OPG's total financial exposure at approximately \$6 billion, a present value amount at April 1, 1999 (approximately \$8.8 billion in 2005 dollars) based on used fuel bundle projections of 2.23 million bundles consistent with the station lives included within the initial financial reference plan. OPG makes quarterly payments to the Used Fuel Fund over the life of its nuclear generating stations, as specified in the ONFA. Required funding for 2005 under the ONFA was \$454 million, including a contribution to The Ontario NFWA Trust (the "Trust"). In 2005, an amount of \$150 million was directed to the Trust to meet the 2005 requirement of \$100 million and \$50 million was directed towards the 2006 requirement.

The NFWA was proclaimed into force in November 2002. In accordance with the NFWA, the Nuclear Waste Management Organization was formed to prepare and review alternatives, and to provide recommendations to the federal government for long-term management of nuclear fuel waste by November 2005. The federal government will select the option for dealing with the long-term management of nuclear fuel waste based on submitted plans. As required under the NFWA, OPG made an initial deposit of \$500 million into the Trust in November 2002. The NFWA also requires OPG to make annual contributions of \$100 million to the Trust, to be deposited into the Trust no later than the November anniversary of the NFWA. To comply with this requirement, OPG contributed \$100 million to the Trust in each of 2003 and 2004 and \$150 million in 2005 (\$50 million funded on December 31, 2005 as part of OPG's \$100 million funding requirement for the November 2005 to November 2006 period). Under the NFWA, OPG must continue to deposit \$100 million annually into the Trust until the federal government has approved a long-term plan. Future contributions to the Trust beyond 2005 will be dependent on the direction chosen by the federal government based on the recommendations submitted in November 2005. Given that the Trust forms part of the Used Fuel Fund, contributions to the Trust, as required by the NFWA, are applied towards the ONFA payment obligations.

As required by the *Nuclear Safety and Control Act* (Canada), and under the terms of the ONFA, the Province issued a guarantee to the Canadian Nuclear Safety Commission ("CNSC"), on behalf of OPG, for up to \$1,510 million. This is a guarantee that there will be sufficient funds available to discharge the current nuclear decommissioning and waste management liabilities. The provincial guarantee will supplement the Used Fuel Fund and the Decommissioning Fund until they have accumulated sufficient funds to cover the accumulated liabilities for nuclear decommissioning and waste management. The guarantee, taken together with the Used Fuel Fund and Decommissioning Fund, was in satisfaction of

OPG's nuclear licensing requirements with the CNSC. OPG pays the Province an annual guarantee fee of 0.5 per cent of the amount guaranteed by the Province. OPG paid the annual guarantee fee for 2005 of \$8 million in the first quarter of 2005.

Under the ONFA, the Province guarantees OPG's annual return in the Used Fuel Fund at 3.25 per cent plus the change in the Ontario Consumer Price Index ("committed return"). The difference between the committed return on the Used Fuel Fund and the actual market return, based on the fair value of fund assets, which includes realized and unrealized returns, is due to or due from the Province. Since OPG accounts for the investments in the segregated funds on an amortized cost basis, the amount due to or due from the Province recorded in the consolidated financial statements is the difference between the committed return and the actual return based on realized returns only. At December 31, 2005, the Used Fuel Fund accounts included an amount due to the Province of \$4 million (2004 – \$4 million). If the investments in the Used Fuel Fund were accounted for at fair market value in the consolidated financial statements, at December 31, 2005, there would be an amount due to the Province of \$306 million (2004 – \$156 million).

Under the ONFA, a rate of return target of 5.75 per cent per annum was established for the Decommissioning Fund, subject to changes in the ONFA Reference Plan. If the rate of return deviates from 5.75 per cent, or if the estimate of the liabilities changes under the current approved ONFA Reference Plan, the Decommissioning Fund may become over or underfunded. Under the ONFA, if there is a surplus in the Decommissioning Fund such that the liabilities, as defined by the Current Approved ONFA Reference Plan, are at least 120 per cent funded, OPG may direct up to 50 per cent of the surplus over 120 per cent as a contribution to the Used Fuel Fund, and the OEFC is entitled to a distribution of an equal amount. In addition, upon termination of the ONFA, the Province has a right to any excess funds, which is the extent to which the fair market value of the Decommissioning Fund exceeds the estimated completion costs approved under the Current Approved ONFA Reference Plan. At December 31, 2005, the balance of the Decommissioning Fund, on an amortized cost basis, exceeded the estimated completion costs under the Current Approved ONFA Reference Plan. The Decommissioning Fund had an excess of \$7 million due to the Province on an amortized cost basis. If the investments in the Decommissioning Fund were accounted for at fair market value in the consolidated financial statements at December 31, 2005, and the Decommissioning Fund was terminated under the ONFA, there would be an amount due to the Province of \$484 million (2004 – \$249 million).

The nuclear fixed asset removal and nuclear waste management funds as at December 31, 2005 and 2004, consist of the following:

<i>(millions of dollars)</i>	Amortized Cost Basis		Fair Value	
	2005	2004	2005	2004
Decommissioning Fund	4,106	3,858	4,583	4,131
Due to Province – Decommissioning Fund	(7)	-	(484)	(249)
	4,099	3,858	4,099	3,882
Used Fuel Fund ¹	2,693	2,122	2,995	2,274
Due (to) from Province – Used Fuel Fund	(4)	(4)	(306)	(156)
	2,689	2,118	2,689	2,118
	6,788	5,976	6,788	6,000

¹ The Ontario NFWA Trust represents \$1,003 million as at December 31, 2005 (2004 – \$794 million) of the Used Fuel Fund on an amortized cost basis.

The amortized cost and fair value of the securities invested in the segregated funds, which include the Used Fuel Fund and Decommissioning Fund, as at December 31, 2005 and 2004 are as follows:

<i>(millions of dollars)</i>	Amortized Cost Basis		Fair Value	
	2005	2004	2005	2004
Cash and cash equivalents and short-term investments	516	211	515	211
Marketable equity securities	3,772	3,056	4,547	3,472
Bonds and debentures	1,757	723	1,762	732
Receivable from the OEFC	759	1,993	759	1,993
Administrative expense payable	(5)	(3)	(5)	(3)
	6,799	5,980	7,578	6,405
Due to Province – Decommissioning Fund	(7)	-	(484)	(249)
Due to Province – Used Fuel Fund	(4)	(4)	(306)	(156)
Total	6,788	5,976	6,788	6,000

The bonds and debentures held in the Used Fuel Fund and the Decommissioning Fund as at December 31, 2005 and 2004 mature according to the following schedule:

<i>(millions of dollars)</i>	Fair Value	
	2005	2004
Less than 1 year	-	-
1 - 5 years	769	259
5 - 10 years	485	233
More than 10 years	508	240
Total maturities of debt securities	1,762	732
Average yield	4.3%	4.1%

The receivable of \$759 million (2004 - \$1,993 million) from the OEFC does not have a specified maturity date. The effective rate of interest on the OEFC receivable was 5.8 per cent in 2005 (2004 – 5.3 per cent).

10. INCOME TAXES

Commencing April 1, 2005, OPG accounts for income taxes related to the rate regulated segments of its business using the taxes payable method. Under the taxes payable method, OPG does not recognize future income taxes related to the rate regulated segments of its business to the extent that the future income taxes are expected to be recovered in the regulated rates charged to future customers. As part of the transition, on April 1, 2005, OPG reversed the net future income tax asset balance of \$74 million relating to the rate regulated segments of its business, and recognized the amount as an extraordinary loss in determining net income. The extraordinary item reduced basic and diluted earnings per share for the year ended December 31, 2005 by \$0.29 per share.

A reconciliation between the statutory and the effective rate of income taxes is as follows:

<i>(millions of dollars)</i>	2005	2004
Income (loss) before income taxes	558	(38)
Combined Canadian federal and provincial statutory income tax rates, including surtax	36.1%	36.1%
Statutory income tax rates applied to accounting income	202	(14)
Increase (decrease) in income taxes resulting from:		
Large corporations tax in excess of surtax	28	30
Lower future tax rate on temporary differences	(12)	(3)
Non-taxable income items	7	(4)
Unrecorded future income tax related to regulated operations	(157)	-
Change in income tax positions	50	-
Change in future income tax asset valuation allowance	-	(93)
Other	-	4
	(84)	(66)
Income tax expense (recovery)	118	(80)
Effective rate of income taxes	21.1%	210.5%

Prior to 2004, OPG had established a valuation allowance of \$93 million to recognize that it was more likely than not that this amount of future income taxes recoverable would not be realized in light of consecutive taxable losses in preceding years. In 2004, the valuation allowance was reduced by \$93 million to nil as a consequence of the introduction of rate regulation. With the intended elimination of the future income tax assets and liabilities of the regulated business upon inception of rate regulation on April 1, 2005, it was expected that there would be a significant future income tax liability position remaining in the unregulated business. This expected future income tax liability position enabled OPG to recognize, in 2004, the \$93 million in future income tax assets. This resulted in a reduction in the 2004 income tax provision which did not occur in 2005.

OPG has taken certain filing positions for corporate income and capital taxes that may be challenged on audit and possibly disallowed and result in a significant increase in the tax obligation upon reassessment. During 2005, OPG recorded an income tax charge of \$50 million to provide for a change in income tax liabilities related to certain income tax positions that the Company has taken in prior years. There is still uncertainty around the amount of the tax provision, and Management is not able to determine the impact of that uncertainty on the consolidated financial statements.

Significant components of the provision for income tax expense (recovery) are presented in the table below:

<i>(millions of dollars)</i>	2005	2004
Current income tax expense	80	21
Future income tax expense (benefits):		
Change in temporary differences	(51)	50
Non-capital loss carry-forward	88	(67)
Valuation allowance (reversal)	-	(93)
Other	1	9
	38	(101)
Income tax expense (recovery)	118	(80)

The income tax effects of temporary differences that give rise to future income tax assets and liabilities are presented in the table below:

<i>(millions of dollars)</i>	2005	2004
Future income tax assets:		
Fixed asset removal and nuclear waste management liabilities	27	2,806
Other liabilities and assets	107	446
Non-capital loss carry-forward	98	168
Future recoverable Ontario minimum tax	37	42
	269	3,462
Future income tax liabilities:		
Fixed assets	351	1,211
Fixed asset removal and nuclear waste management fund	-	2,039
Other liabilities and assets	141	323
	492	3,573
Net future income tax liabilities	223	111
Represented by:		
Current portion (asset)	(18)	(44)
Long-term portion	241	155
	223	111

The following table summarizes the consolidated statement of income and balance sheet amounts under the method used by the Company to account for income taxes compared to what would have been reported had OPG applied the liability method for the regulated business for 2005:

<i>(millions of dollars)</i>	As Stated	Liability Method
Future income tax expense	38	195
Extraordinary item	74	-
Current portion (assets)	(18)	(38)
Long-term portion	241	344

Had OPG continued to use the liability method of accounting for income taxes for the regulated business, the future tax expense for the year ended December 31, 2005 would have increased by \$157 million with a corresponding increase in the future income tax liability.

At December 31, 2005, OPG had available approximately \$280 million (2004 – \$549 million) of non-capital loss carry-forwards. The non-capital loss carry-forward is related to the following taxation years:

<i>(millions of dollars)</i>	Loss-Carry Forward	Expiry Date
2003	33	2010
2004	247	2014

The amount of cash income taxes paid during 2005 was \$20 million (2004 – \$17 million).

11. BENEFIT PLANS

The post employment benefit programs include pension, group life insurance, health care and long-term disability benefits. The registered pension plan is a contributory defined benefit plan covering most employees and retirees. Pension fund assets include equity securities and corporate and government debt securities, real estate and other investments which are managed by professional investment managers. The fund does not invest in equity or debt securities issued by OPG. The supplementary pension plans are defined benefit plans covering certain employees and retirees.

Pension and OPEB obligations are impacted by factors including interest rates, adjustments arising from plan amendments, changes in assumptions and experience gains or losses. The pension and OPEB obligations, and the pension fund assets, are measured at December 31, 2005.

	Registered and Supplementary Pension Plans		Other Post Employment Benefits	
	2005	2004	2005	2004
<i>Weighted Average Assumptions – Benefit Obligation at Year End</i>				
Rate used to discount future benefits	5.00%	6.00%	4.97%	5.88%
Salary schedule escalation rate	3.00%	3.25%	-	-
Rate of cost of living increase to pensions	2.00%	2.25%	-	-
Initial health care trend rate	-	-	7.76%	7.03%
Ultimate health care trend rate	-	-	4.68%	4.46%
Year ultimate rate reached	-	-	2014	2014
Rate of increase in disability benefits	-	-	2.00%	2.25%

	Registered and Supplementary Pension Plans		Other Post Employment Benefits	
	2005	2004	2005	2004
<i>Weighted Average Assumptions – Cost for the Year</i>				
Expected return on plan assets net of expenses	7.00%	7.00%	-	-
Rate used to discount future benefits	6.00%	6.25%	5.88%	6.17%
Salary schedule escalation rate	3.25%	3.25%	-	-
Rate of cost of living increase to pensions	2.25%	2.25%	-	-
Initial health care trend rate	-	-	7.03%	6.33%
Ultimate health care trend rate	-	-	4.46%	4.46%
Year ultimate rate reached	-	-	2014	2010
Rate of increase in disability benefits	-	-	2.25%	2.25%
Average remaining service life for employees (years)	11	12	11	12

	Registered Pension Plan		Supplementary Pension Plans		Other Post Employment Benefits	
	2005	2004	2005	2004	2005	2004
<i>(millions of dollars)</i>						
<i>Changes in Plan Assets</i>						
Fair value of plan assets at beginning of year	7,056	6,449	-	-	-	-
Contributions by employer	254	154	7	6	58	54
Contributions by employees	56	52	-	-	-	-
Actual return on plan assets net of expenses	858	693	-	-	-	-
Settlements	(2)	(4)	-	-	-	-
Benefit payments	(301)	(288)	(7)	(6)	(58)	(54)
Fair value of plan assets at end of year	7,921	7,056	-	-	-	-
<i>Changes in Projected Benefit Obligation</i>						
Projected benefit obligation at beginning of year	7,663	7,046	144	117	1,499	1,307
Employer current service costs	163	143	7	8	47	41
Contributions by employees	56	52	-	-	-	-
Interest on projected benefit obligation	461	442	9	7	88	82
Past service costs	-	-	-	-	1	-
Curtailment loss (gain)	-	2	-	-	-	(1)
Settlement gain	(2)	(4)	-	-	-	-
Benefit payments	(301)	(288)	(7)	(6)	(58)	(54)
Net actuarial loss (gain)	1,055	270	(9)	18	488	124
Projected benefit obligation at end of year	9,095	7,663	144	144	2,065	1,499
Funded Status – Deficit at end of year	(1,174)	(607)	(144)	(144)	(2,065)	(1,499)

	2005	2004
Registered pension plan fund asset investment categories		
Equities	64%	65%
Fixed income	33%	33%
Cash and short-term	3%	2%
Total	100%	100%

The assets of the OPG pension fund are allocated among three principal investment categories. Furthermore, equity investments are diversified across Canadian, U.S. and non-North American stocks. The fund also has a small real estate portfolio that is less than one per cent of plan assets.

Based on the most recently filed actuarial valuation, as at January 1, 2005, there was an unfunded liability on a going-concern basis of \$465 million and a deficiency on a wind-up basis of \$1,979 million. In the previously filed actuarial valuation, as at April 1, 2002, there was a surplus of \$262 million on a going-concern basis and \$204 million on a wind-up basis.

The supplementary plans are not funded, but are secured by letters of credit totalling \$138 million (2004 – \$125 million).

	Registered Pension Plan		Supplementary Pension Plans		Other Post Employment Benefits	
	2005	2004	2005	2004	2005	2004
<i>(millions of dollars)</i>						
<i>Reconciliation of Funded Status to Accrued Benefit Asset (Liability)</i>						
Funded status – deficit at end of year	(1,174)	(607)	(144)	(144)	(2,065)	(1,499)
Unamortized net actuarial loss	1,737	1,012	18	28	885	422
Unamortized past service costs	100	119	4	5	16	18
Accrued benefit asset (liability) at end of year	663	524	(122)	(111)	(1,164)	(1,059)
Short-term portion	-	-	(7)	(6)	(67)	(59)
Long-term portion	663	524	(115)	(105)	(1,097)	(1,000)

	Registered Pension Plan		Supplementary Pension Plans		Other Post Employment Benefits	
	2005	2004	2005	2004	2005	2004
<i>(millions of dollars)</i>						
<i>Components of Cost Recognized</i>						
Current service costs	163	143	7	8	47	41
Interest on projected benefit obligation	461	442	9	7	88	82
Expected return on plan assets net of expenses	(527)	(511)	-	-	-	-
Curtailment loss (gain)	-	2	-	-	-	(1)
Amortization of past service costs	18	18	1	1	3	3
Amortization of net actuarial loss	-	-	1	-	25	15
Cost recognized	115	94	18	16	163	140

	Registered Pension Plan		Supplementary Pension Plans		Other Post Employment Benefits	
<i>(millions of dollars)</i>	2005	2004	2005	2004	2005	2004
<i>Components of Cost Incurred and Recognized</i>						
Current service costs	163	143	7	8	47	41
Interest on projected benefit obligation	461	442	9	7	88	82
Actual return on plan assets net of expenses	(858)	(693)	-	-	-	-
Curtailment loss (gain)	-	2	-	-	-	(1)
Past service costs	-	-	-	-	1	-
Net actuarial loss (gain)	1,055	270	(9)	18	488	124
Cost incurred in year	821	164	7	33	624	246
Differences between costs incurred and recognized in respect of:						
Actual return on plan assets net of expenses	331	182	-	-	-	-
Past service costs	18	18	1	1	2	3
Net actuarial (gain) loss	(1,055)	(270)	10	(18)	(463)	(109)
Cost recognized	115	94	18	16	163	140

A one per cent increase or decrease in the health care trend rate would result in an increase in the service and interest components of the 2005 OPEB cost recognized of \$26 million (2004 – \$21 million) or a decrease in the service and interest components of the 2005 OPEB cost recognized of \$20 million (2004 – \$19 million), respectively. A one per cent increase or decrease in the health care trend rate would result in an increase in the projected OPEB obligation at December 31, 2005 of \$343 million (2004 – \$221 million) or a decrease in the projected OPEB obligation at December 31, 2005 of \$266 million (2004 – \$175 million).

12. FINANCIAL INSTRUMENTS

Fair values of derivative instruments have been estimated by reference to quoted market prices for actual or similar instruments where available. Where quoted market prices are not available, OPG considers various factors to estimate forward prices, including market prices and price volatility in neighbouring electricity markets, market prices for fuel, and other factors.

Trading activities and liquidity in the Ontario electricity market have been limited as companies are generally entering only into short-term contracts. As a result, forward pricing information for contracts may not accurately represent the cost to enter into these contracts. For Ontario-based contracts that are not entered into for hedging purposes, OPG established liquidity reserves against the fair market value of the assets and liabilities equal to the gain or loss on these contracts. These reserves increased trading revenue by \$4 million during 2005 (2004 – decreased by \$2 million). Contracts for transactions outside of Ontario continue to be carried on the consolidated balance sheets as assets or liabilities at fair value, with changes in fair value recorded in trading revenue as gains or losses.

Derivative Instruments Used for Hedging Purposes

The following table provides the estimated fair value of derivative instruments designated as hedges. The majority of OPG's derivative instruments are treated as hedges, with gains or losses recognized upon settlement when the underlying transactions occur. OPG holds financial commodity derivatives primarily to hedge the commodity price exposure associated with changes in the price of electricity.

<i>(millions of dollars except where noted)</i>	Notional Quantity	Terms 2005	Fair Value	Notional Quantity	Terms 2004	Fair Value
(Loss)						
Electricity derivative instruments	4.1 TWh	1-2 yrs	(125)	10.4 TWh	1-3 yrs	(71)
Foreign exchange derivative instruments	U.S. \$15	Jan/06	-	U.S. \$10	Jan/05	-
Interest rate hedges	400	1-15 yrs	(7)	-	-	-

OPG entered into a number of forward start interest rate swap agreements to hedge against the effect of future interest rate movement based on the anticipated future borrowing requirement for the Niagara tunnel project. These transactions are ordinarily accounted for as hedges, however, approximately \$5 million was charged to current period operations for those hedges that did not meet the effectiveness criteria during 2005. The remaining loss was deferred.

Foreign exchange derivative instruments are used to hedge the exposure to anticipated U.S. dollar denominated purchases. The weighted average fixed exchange rate for contracts outstanding at December 31, 2005 was U.S. \$0.87 (2004 – U.S. \$0.81) for every Canadian dollar.

Derivative Instruments Not Used for Hedging Purposes

The carrying amount (fair value) of derivative instruments not designated for hedging purposes is as follows:

<i>(millions of dollars except where noted)</i>	Notional Quantity	Fair Value	Notional Quantity	Fair Value
	2005		2004	
Foreign exchange derivative	U.S. \$3	-	-	-
Commodity derivative instruments				
Assets	3.3 TWh	13	7.9 TWh	12
Liabilities	1.1 TWh	(37)	1.3 TWh	(12)
		(24)		-
Ontario market liquidity reserve		(3)		(7)
Total		(27)		(7)

Foreign exchange derivative instruments that are not designated as hedges have a weighted average exchange rate of U.S. \$0.85.

Fair Value of Other Financial Instruments

The carrying values of cash and cash equivalents, accounts receivable, accounts payable and accrued charges, Market Power Mitigation Agreement rebate payable, short-term notes payable, and long-term debt due within one year approximate their fair values due to the immediate or short-term maturity of these financial instruments. Fair values for other financial instruments have been estimated by reference to quoted market prices for actual or similar instruments where available.

The carrying values and fair values of these other financial instruments are as follows:

<i>(millions of dollars)</i>	Carrying Value 2005	Fair Value	Carrying Value 2004	Fair Value
Financial Assets				
Nuclear fixed asset removal and nuclear waste management funds	6,788	6,788	5,976	6,000
Long-term accounts receivable and other assets	61	61	56	56
Financial Liabilities				
Long-term debt	3,895	4,081	3,404	3,582
Long-term accounts payable and accrued charges	183	183	212	212

Credit Risk

Credit risk is the financial risk of non-performance by contractual counterparties. Credit risk excludes any operational risk resulting from a third party failing to deliver a product or service as expected. OPG derives revenue from several other sources including the sale of energy products and financial risk management products to third parties. However, the majority of OPG revenues are derived from sales through the IESO administered spot market.

Credit exposure to the IESO fluctuates based on spot prices and the volume of rate regulated and unregulated generation, and is reduced each month upon settlement of the accounts. Credit exposure to the IESO peaked at \$1,146 million during the year ended December 31, 2005 and at \$901 million during the year ended December 31, 2004.

13. COMMON SHARES

As at December 31, 2005 and 2004, OPG had 256,300,010 common shares issued and outstanding at a stated value of \$5,126 million. OPG is authorized to issue an unlimited number of common shares without nominal or par value.

14. COMMITMENTS AND CONTINGENCIES

Litigation

Various legal proceedings are pending against OPG or its subsidiaries covering a wide range of matters that arise in the ordinary course of its business activities. OPG had become aware of a class action suit for \$50 billion, relating to alleged negative health impacts caused by burning coal to generate electricity, that has been issued in an Ontario Court naming OPG and 20 U.S.-based electricity generators as defendants. Although the claim was filed in the court office, it has not been served on OPG and, the time allowed to the plaintiff to serve the claim has expired. While the court has discretion to extend the time for service upon a motion by the Plaintiffs, OPG does not believe this is likely. The preliminary assessment is that the claim would be unlikely to succeed even if the Plaintiffs further pursued the claim.

In July 2004, OPG and two individual OPG employees were each charged with criminal negligence causing death and criminal negligence causing bodily harm in relation to a 2002 drowning accident at Barrett Chute. The trial commenced on January 16, 2006, and is expected to last approximately four to six months.

Also, certain First Nations have commenced actions for interference with reserve and traditional land rights. The claims by some of these First Nations total approximately \$50 million and claims by others are for unspecified amounts.

Each of these matters is subject to various uncertainties. Some of these matters may be resolved unfavourably with respect to OPG and could have a significant effect on OPG's financial position. Management has provided for contingencies that are determined to be likely and are responsibly measurable.

Environmental

OPG was required to assume certain environmental obligations from Ontario Hydro. A provision of \$76 million was established as at April 1, 1999 for such obligations. During the year ended December 31, 2005, expenditures of \$4 million (2004 – \$2 million) were recorded against the provision.

Current operations are subject to regulation with respect to air, soil and water quality and other environmental matters by federal, provincial and local authorities. The cost of obligations associated with current operations is provided for on an ongoing basis. Management believes it has made adequate provision in its consolidated financial statements to meet OPG's current environmental obligations.

Guarantees

As part of normal business, OPG and certain of its subsidiaries enter into various agreements providing financial or performance assurance to third parties on behalf of certain subsidiaries. Such agreements include guarantees, standby Letters of Credit and surety bonds.

Contractual and Commercial Commitments

The Company's contractual obligations and other significant commercial commitments as at December 31, 2005 are as follows:

<i>(millions of dollars)</i>	2006	2007	2008	2009	2010	Thereafter	Total
Contractual obligations:							
Fuel supply agreements	693	425	197	68	15	15	1,413
Contributions under ONFA	454	454	679	350	350	1,403	3,690
Long-term debt repayment	800	400	400	350	970	775	3,695
Interest on long-term debt	214	168	145	122	90	55	794
Unconditional purchase obligations	26	20	12	9	15	27	109
Long-term accounts payable	28	28	9	-	-	-	65
Operating lease obligations	13	13	13	13	14	-	66
Pension contributions ¹	254	-	-	-	-	-	254
Other	75	34	35	34	35	11	224
Significant commercial commitments:							
Niagara Tunnel	158	173	172	116	1	-	620
Total	2,715	1,715	1,662	1,062	1,490	2,286	10,930

¹ The pension contributions include additional funding requirements towards the deficit and ongoing funding requirements in accordance with the actuarial valuation as at January 1, 2005. The contributions are affected by various factors including market performance, changes in actuarial assumptions, plan experience, and the timing of funding valuations. Funding requirements after 2006 are excluded due to significant variability in the assumptions required to project the timing of future cash flows.

In June 2004, OPG announced and the Government of Ontario ("Government") endorsed the decision to proceed with a new water diversion tunnel that will increase the amount of water flowing to existing turbines at the Sir Adam Beck generating stations in Niagara. This tunnel will allow the Beck generating facilities to utilize available water more effectively, and is expected to increase annual generation on average by about 1.6 TWh. OPG awarded a contract to Strabag AG in August 2005 to design and construct the 10.4 kilometre tunnel and associated facilities. The value of the design-build contract is approximately \$600 million, with the total project expected to cost approximately \$985 million. Construction started in September 2005. Project completion is expected by late 2009.

Other Commitments

In addition to the above commitments, the Company has the following commitments:

The Company maintains labour agreements with the Power Workers' Union ("PWU"). The agreement is effective from April 1, 2002 to March 31, 2006. OPG and the PWU recently reached tentative agreements, which are subject to membership ratification. The Company also maintains a labour agreement with the Society of Energy Professionals. The agreement is effective from January 1, 2005 to December 31, 2005. The agreement has since been renewed and extended to December 31, 2010. As of December 31, 2005, the Company had approximately 90 per cent of its regular labour forces covered by collective bargaining agreements.

Contractual and commercial commitments above exclude certain purchase orders as they represent purchase authorizations rather than legally binding contracts and are subject to change without significant penalties.

Proxy Property Taxes

In November 2005, OPG received a letter from the Ministry of Finance indicating its intent to recommend to the Minister of Finance that an Ontario regulation covering proxy property taxes be updated retroactive to April 1, 1999 to reflect reassessments and appeal settlements of certain OPG properties since that date. Updates to the regulation may not occur for up to two years. OPG has not recorded any amounts relating to this anticipated regulation change.

15. RESTRUCTURING

The change in the restructuring liability for termination benefits for 2005 and 2004 is as follows:

<i>(millions of dollars)</i>	2005	2004
Liability, beginning of year	20	52
Restructuring charges	10	19
Payments	(18)	(51)
Liability, end of year	12	20

During 2004, OPG recorded restructuring charges of \$16 million, which consisted of \$15 million for termination benefits and \$1 million in related pension and OPEB expenses associated with its Lakeview generating station. OPG also recorded restructuring charges of \$4 million related to its Energy Marketing business during 2004. During 2005, OPG recorded restructuring charges of \$10 million which consisted of \$4 million related to the Lakeview generating station and \$6 million related to the Energy Markets business.

16. TRANSITION RATE OPTION CONTRACTS

Under regulation known as Transition – Generation Corporation Designated Rate Options (“TRO”), OPG has been required to provide transitional price relief since market opening to certain power customers for up to four years based on the consumption and average price paid by each customer during a reference period of July 1, 1999 to June 30, 2000. The TRO is treated as a hedge of generation revenue. The maximum anticipated volume subject to the transitional price relief was approximately 5.4 TWh in the first year after market opening and 3.6 TWh in the second year. The maximum anticipated volume in each of the third and fourth years is 1.8 TWh. The maximum length of the program is four years, which expires April 30, 2006.

A provision of \$210 million on the TRO contracts was recorded in the first quarter of 2002 based on the estimated future loss on these contracts. The provision was determined at that time using management’s best estimates of the forward price curve for electricity, wholesale electricity market fees, impact of decontrol on these contracts, interruptions of volume, and the recovery of Market Power Mitigation Agreement rebates. The provision for the TRO contracts was established based on meeting decontrol targets within three years of market opening. An additional charge of \$30 million related to the fourth year of the TRO contracts was recorded in 2003, based on OPG’s expectation that the Company would not meet the decontrol targets necessary for TRO contracts to expire after three years.

The change in the TRO contracts provision for the years ended December 31, 2005 and 2004 is as follows:

<i>(millions of dollars)</i>	2005	2004
Provision, beginning of year	48	100
Decrease of provision during the year	(36)	(52)
Provision, end of year	12	48

17. MARKET POWER MITIGATION AGREEMENT REBATE

Until April 1, 2005, OPG was required under its generating licence to comply with prescribed market power mitigation measures to address the potential for OPG to exercise market power in Ontario. The market power mitigation measures included both a rebate mechanism and the requirement to decontrol generating capacity. Under the rebate mechanism, a majority of OPG's expected energy sales in Ontario were subject to an average annual revenue cap of 3.8¢/kWh. During the term of the Market Power Mitigation Agreement, OPG was required to pay a rebate to the Independent Electricity System Operator equal to the excess, if any, of the average hourly spot energy price over 3.8¢/kWh for a 12-month settlement period, multiplied by the amount of energy subject to the rebate mechanism. The Market Power Mitigation Agreement was replaced effective April 1, 2005 by a regulated price for baseload hydroelectric and nuclear generation and a revenue limit that applies to OPG's unregulated generation assets.

In accordance with the Market Power Mitigation Agreement, the rebate was calculated after taking into account the amount of energy sales subject to the rebate mechanism for only those generating stations that OPG continues to control. Since the average hourly spot price during the three months ended March 31, 2005, when the rebate mechanism ended, exceeded the 3.8¢/kWh revenue cap, OPG provided \$412 million (2004 – \$1,154 million) as a Market Power Mitigation Agreement rebate.

The change in the Market Power Mitigation Agreement rebate liability for the years ended December 31, 2005 and 2004 is as follows:

<i>(millions of dollars)</i>	2005	2004
Liability, beginning of year	439	409
Increase to provision during the year	412	1,154
Payments	(851)	(1,124)
Liability, end of year	-	439

18. REVENUE LIMIT REBATE

Eighty-five per cent of the generation output from OPG's unregulated generation assets, excluding the Lennox generating station, TRO volumes and forward sales as of January 1, 2005, is subject to a revenue limit based on an average price of \$47.00/MWh (4.7¢/kWh). This revenue limit was originally established for a period of 13 months ending April 30, 2006. The Government has recently announced the extension of the revenue limit for an additional three years. Starting May 1, 2006, the revenue limit will decrease to 4.6¢/kWh from the present limit of 4.7¢/kWh. On April 1, 2007, the revenue limit will return to 4.7¢/kWh and increase to 4.8¢/kWh effective April 1, 2008. Revenues above these limits will be returned to the Independent Electricity System Operator ("IESO"), and the IESO will subsequently issue a rebate to consumers.

The change in the revenue limit rebate liability for the year ended December 31, 2005 is as follows:

<i>(millions of dollars)</i>	2005
Liability, beginning of year	-
Increase to provision during the year	739
Payments	-
Liability, end of year	739

19. BUSINESS SEGMENTS

A regulation made pursuant to the *Electricity Restructuring Act, 2004* provided that OPG would receive regulated prices for its baseload hydroelectric and nuclear facilities. These initial prices took effect April 1, 2005, and are expected to remain in effect until at least March 31, 2008, at which time it is anticipated that the OEB will have established new regulated prices. Given the effective date of these prices, and OPG's management approach, OPG changed its definition of business segments on April 1, 2005 from Generation and Energy Marketing to Regulated – Nuclear, Regulated – Hydroelectric and Unregulated Generation. OPG will continue to report other activities, including the previously separately presented trading activities in the Other category. As a result of this change in definition, OPG has reclassified the comparative periods to be consistent with the current presentation of business segments.

Regulated – Nuclear Segment

OPG's Regulated – Nuclear business segment operates in Ontario, generating and selling electricity from the nuclear generating stations that it owns and operates. The business segment includes electricity generated by the Pickering A and B, and Darlington nuclear generating stations.

OPG's Regulated – Nuclear business segment includes revenue under the terms of a lease arrangement with Bruce Power related to the Bruce nuclear generating stations. The arrangement includes lease revenue, interest income and revenue from engineering analysis and design, technical and other services. The Regulated – Nuclear business segment also includes revenue earned from isotope sales and ancillary services. Ancillary revenues are earned through voltage control/reactive support. These earnings are included in the Regulated – Nuclear business segment since they were included in determining the regulated price for production from the nuclear facilities.

Bruce Nuclear Generating Stations

In May 2001, the Company leased its Bruce A and Bruce B nuclear generating stations to Bruce Power until 2018, with options to renew for up to 25 years.

Under the terms of the lease, OPG agreed to transfer certain fuel and material inventory to Bruce Power, in addition to certain fixed assets. Pension assets and liabilities related to the approximately 3,000 employees were transferred to Bruce Power. Bruce Power assumed the liability for other post employment benefits for these employees. OPG makes payments to Bruce Power in respect of other post employment benefits of approximately \$2.3 million per month over a 72-month period, ending in 2008.

As part of the closing, OPG recorded deferred revenue to reflect the initial payments of \$595 million less net assets transferred to Bruce Power under the lease agreement. The deferred revenue is being amortized over the initial lease term of approximately 18 years and is recorded as revenue.

In December 2002, British Energy plc, entered into an agreement to dispose of its entire 82.4 per cent interest in Bruce Power. The transaction was completed in February 2003 and a consortium of Canadian

companies assumed the lease of the Bruce A and Bruce B nuclear generating stations that was formerly held by British Energy plc. The Bruce facilities will continue to be operated by Bruce Power. Upon closing of the transaction, the \$225 million note receivable was paid to OPG, and lease payments commenced to be paid monthly. Proceeds from the note are to be applied by March 2008 against OPG's funding requirements with respect to the nuclear fixed asset removal and nuclear waste management liabilities.

As part of the agreement reached in October 2005 between the Province and Bruce Power, OPG received a Shareholder Declaration from the Province instructing OPG's Board of Directors to accept certain amendments to the lease agreement. These amendments included a change to the provisions regarding the transfer of Bruce Power's interest in the site and included a reduction of the annual lease payment for three of the four refurbished Bruce A units to \$5.5 million per unit (in 2002 dollars, escalated at CPI), after the planned future refurbishments are completed. These changes to the lease agreement will impact OPG when Units 1 and 2 of the Bruce A nuclear generating station are returned to service, and when Unit 3 is refurbished at the end of its current operational life. Other changes to the existing arrangements were made to address Cameco Corporation's decision not to participate in the refurbishment of the Bruce A nuclear generating station.

For 2004 through 2008, minimum payments under the lease are \$190 million annually, subject to limited exceptions. The lease revenue of \$244 million (2004 – \$236 million) was recorded in revenue. The remaining terms of the operating lease agreement will remain substantially unchanged until the planned future refurbishments are completed.

The net book value of fixed assets on lease to Bruce power including costs relating to refurbishing and restarting Bruce A at December 31, 2005, was \$492 million (2004 – \$590 million).

Regulated – Hydroelectric Segment

OPG's Regulated – Hydroelectric business segment operates in Ontario, generating and selling electricity from its baseload hydroelectric generating stations. The business segment includes electricity generated by the Sir Adam Beck 1, 2 and Pump generating station, DeCew Falls 1 and 2, and the R.H. Saunders hydroelectric facilities. The Regulated – Hydroelectric business segment also includes ancillary revenues related to these stations earned through offering available generating capacity as operating reserve and through the supply of other ancillary services including voltage control/reactive support, certified black start facilities and automatic generation control.

Unregulated Generation Segment

OPG's Unregulated Generation business segment operates in Ontario, generating and selling electricity from its fossil-fuelled generating stations and from the hydroelectric generating stations not included in the Regulated – Hydroelectric segment. The Unregulated Generation business segment also includes ancillary revenues earned through offering available generating capacity as operating reserve, and through the supply of other ancillary services including voltage control/reactive support, certified black start facilities and automatic generation control, and revenues from other services.

Other

OPG earns revenue from its joint venture share of the Brighton Beach Power Limited Partnership ("Brighton Beach") related to an energy conversion agreement between Brighton Beach and Coral Energy Canada Inc. ("Coral"). In addition, the Other category includes revenue from real estate rentals.

The revenue and expenses related to OPG's trading and other non-hedging activities are also included in the Other category. As part of these activities, OPG transacts with counterparties in Ontario and neighbouring energy markets in predominantly short-term trading activities of typically one year or less in duration. These activities relate primarily to physical energy that is purchased and sold at the Ontario border, sales of financial risk management products and sales of energy-related products. All contracts that are not designated as hedges are recorded as assets or liabilities at fair value, with changes in fair value recorded in other revenue as gains or losses.

Segment Income for year ended December 31, 2005	Regulated – Nuclear	Regulated – Hydroelectric	Unregulated Generation	Other	Total
<i>(millions of dollars)</i>					
Revenues					
Revenue	2,607	857	3,399	86	6,949
Market Power Mitigation Agreement rebate	(160)	(65)	(187)	-	(412)
Revenue limit rebate	-	-	(739)	-	(739)
	2,447	792	2,473	86	5,798
Fuel expense	115	254	928	-	1,297
Gross margin	2,332	538	1,545	86	4,501
Operations, maintenance and administration	1,788	77	594	57	2,516
Depreciation and amortization	374	68	276	35	753
Accretion on fixed asset removal and nuclear waste management liabilities	467	-	9	-	476
Earnings on nuclear fixed asset removal and nuclear waste management funds	(381)	-	-	-	(381)
Property and capital taxes	31	18	54	4	107
Restructuring	-	-	4	6	10
Income (loss) before the following: Impairment of long-lived assets	53	375	608	(16)	1,020
	63	-	202	-	265
(Loss) income before interest, income taxes and extraordinary item	(10)	375	406	(16)	755

Segment Income for year ended December 31, 2004	Regulated – Nuclear	Regulated – Hydroelectric	Unregulated Generation	Other	Total
<i>(millions of dollars)</i>					
Revenues					
Revenue	2,421	1,018	2,528	105	6,072
Market Power Mitigation Agreement rebate	(374)	(194)	(586)	-	(1,154)
Revenue limit rebate	-	-	-	-	-
	2,047	824	1,942	105	4,918
Fuel expense	108	255	790	-	1,153
Gross margin	1,939	569	1,152	105	3,765
Operations, maintenance and administration excluding Pickering A return to service	1,611	74	576	62	2,323
Pickering A return to service	271	-	-	-	271
Depreciation and amortization	360	71	302	32	765
Accretion on fixed asset removal and nuclear waste management liabilities	445	-	8	-	453
Earnings on nuclear fixed asset removal and nuclear waste management funds	(313)	-	-	-	(313)
Property and capital taxes	33	18	38	14	103
Restructuring	-	-	16	4	20
Other income	-	-	-	(8)	(8)
(Loss) income before interest, and income taxes	(468)	406	212	1	151

<i>(millions of dollars)</i>	Regulated – Nuclear	Regulated – Hydroelectric	Unregulated Generation	Other	Total
Selected Balance Sheet Information					
December 31, 2005 Segment property, plant and equipment, net	3,156	4,054	3,607	595	11,412
December 31, 2004 Segment property, plant and equipment, net	3,305	4,015	3,986	634	11,940
Selected Cash Flow Information					
Year ended December 31, 2005 Capital expenditures	273	101	90	34	498
Year ended December 31, 2004 Capital expenditures	365	25	78	93	561

20. RELATED PARTY TRANSACTIONS

Given that the Province owns all of the shares of OPG, related parties include the Province, the other successor entities of Ontario Hydro, including Hydro One Inc. ("Hydro One"), the IESO, and the OEFC. OPG also enters into related party transactions with its joint ventures. The transactions between OPG and related parties are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

These transactions are summarized below:

<i>(millions of dollars)</i>	Revenues	Expenses	Revenues	Expenses
	2005		2004	
Hydro One				
Electricity sales	40	-	40	-
Services	-	12	-	12
Settlement Transactions	-	27	-	33
Province of Ontario				
GRC water rentals and land tax	-	132	-	152
Guarantee fee	-	8	-	8
Used Fuel Fund rate of return guarantee	-	-	-	14
Decommissioning Fund excess funding	-	7	-	-
Other	-	-	-	2
OEFC				
GRC and proxy property tax	-	207	-	214
Interest income on receivable	-	(75)	-	(101)
Interest expense on long-term notes	-	211	-	191
Capital tax	-	51	-	49
Income taxes	-	192	-	(80)
Indemnity fees	-	5	-	5
IESO				
Electricity sales	6,517	329	5,465	304
Market Power Mitigation Agreement rebate	(412)	-	(1,154)	-
Revenue limit rebate	(739)	-	-	-
Ancillary services	68	-	90	-
Other	-	-	1	1
	5,474	1,106	4,442	804

At December 31, 2005, accounts receivable included \$14 million (2004 – \$14 million) due from Hydro One and \$324 million (2004 – \$158 million) due from the IESO. Accounts payable and accrued charges at December 31, 2005 included \$2 million (2004 – \$3 million) due to Hydro One.

21. JOINT VENTURES

Significant joint ventures include Brighton Beach Power L.P., which is 50 per cent owned by OPG (2004 – 50 per cent).

The following condensed information from the consolidated statements of operations, cash flows and balance sheets detail the Company's share of its investment in joint ventures and partnerships that have been proportionately consolidated:

<i>(millions of dollars)</i>	2005	2004
Proportionate joint venture operations		
Operating revenue	46	28
Operating expenses	(36)	(22)
Net income	10	6
Proportionate joint venture cash flows		
Operating activities	21	4
Investing activities	(2)	(34)
Financing activities	(4)	32
Share of increase in cash	15	2
Proportionate joint venture balance sheets		
Current assets	26	16
Long-term assets	279	286
Current liabilities	(11)	(5)
Long-term liabilities	(199)	(202)
Share of net assets	95	95

22. INVESTMENT COMPANY

The Company applied AcG-18 for all investments owned by OPGV in 2005. OPGV is a wholly owned subsidiary of the Company and its results are consolidated into the Company's financial statements. Since OPGV is the only enterprise in the group that satisfies the criteria set out in AcG-18, all other investments made by OPG and its subsidiaries, partnerships or joint ventures continue to be carried at amortized cost. The carrying amount of OPGV's investments was \$29 million (2004 – \$36 million) and the amount was included as long-term accounts receivable and other assets on the consolidated balance sheets.

As a result of the application of this policy, the Company's net income for 2005 decreased by \$11 million and other assets decreased by the same amount. The gross unrealized gains and losses on the investment held by OPGV as at December 31, 2005 were \$2 million and \$13 million respectively.

23. RESEARCH AND DEVELOPMENT

For the year ended December 31, 2005, \$19 million (2004 – \$21 million) of research and development expenses were charged to operations.

24. OTHER INCOME

There was no other income recorded in 2005. Other income of \$8 million in 2004 was comprised of \$3 million from the sale of assets and \$5 million from a favourable pension liability settlement.

25. CHANGES IN NON-CASH WORKING CAPITAL BALANCES

<i>(millions of dollars)</i>	2005	2004
Accounts receivable	(191)	(15)
Income taxes recoverable	-	16
Fuel inventory	(12)	(45)
Materials and supplies	(23)	(19)
Market Power Mitigation Agreement rebate payable	(439)	30
Revenue limit rebate payable	739	-
Accounts payable and accrued charges	10	(78)
Income and capital taxes payable	69	12
	153	(99)