

## **MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING**

The accompanying consolidated financial statements of Ontario Power Generation Inc. ("OPG" or the "Company") are the responsibility of management and have been prepared in accordance with Canadian generally accepted accounting principles. Where alternative accounting methods exist, management has selected those it considers most appropriate in the circumstances. The preparation of the consolidated financial statements necessarily involves the use of estimates based on management's judgement, particularly when transactions affecting the current accounting period cannot be finalized with certainty until future periods. The consolidated financial statements have been properly prepared within reasonable limits of materiality.

Management maintains a system of internal controls which are designed to provide reasonable assurance that the financial information is relevant, reliable and accurate, and that OPG's assets are safeguarded and transactions are executed in accordance with management's authorization. These systems are monitored and evaluated by management and by an internal audit service and risk management function.

The Audit and Risk Committee meets regularly with management, internal audit services and the independent external auditors to satisfy itself that each group has properly discharged its respective responsibility, and to review the consolidated financial statements and independent Auditors' Report, and to discuss significant financial reporting issues and auditing matters before recommending approval of the consolidated financial statements by the Board of Directors.

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 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.

**Richard Dicerni (signed)**  
*Acting President and Chief Executive Officer*

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

March 23, 2005

# **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, 2004 and 2003 and the consolidated statements of income (loss), retained earnings 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, 2004 and 2003 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  
March 23, 2005

## CONSOLIDATED STATEMENTS OF INCOME (LOSS)

### Years Ended December 31

(millions of dollars except where noted)

	2004	2003
<b>Revenue</b>		
Revenue before Market Power Mitigation Agreement rebate	6,072	6,688
Market Power Mitigation Agreement rebate	(1,154)	(1,510)
	<b>4,918</b>	5,178
Fuel expense	1,153	1,678
<b>Gross margin</b>	<b>3,765</b>	3,500
<b>Expenses</b>		
Operations, maintenance and administration	2,594	2,393
Depreciation and amortization (note 5)	765	603
Accretion on fixed asset removal and nuclear waste management liabilities	453	430
Earnings on nuclear fixed asset removal and nuclear waste management funds	(313)	(238)
Property and capital taxes	103	114
Loss on transition rate option contracts (note 15)	-	30
	<b>3,602</b>	3,332
<b>Income before the following</b>	<b>163</b>	168
Restructuring (note 14)	20	-
Impairment of long-lived assets (note 5)	-	576
Other income (note 20)	(8)	(58)
Net interest expense	189	144
<b>(Loss) before income taxes</b>	<b>(38)</b>	(494)
Income tax expenses (recoveries) (note 11)		
Current	21	80
Future	(101)	(83)
	<b>(80)</b>	(3)
<b>Net income (loss)</b>	<b>42</b>	(491)
<b>Basic and diluted income (loss) per common share (dollars)</b>	<b>0.16</b>	(1.92)
<b>Common shares outstanding (millions)</b>	<b>256.3</b>	256.3

## CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

### Years Ended December 31

(millions of dollars)

	2004	2003
<b>(Deficit) retained earnings, beginning of year</b>	<b>(147)</b>	361
Net income (loss)	42	(491)
Dividends	-	(17)
<b>(Deficit), end of year</b>	<b>(105)</b>	(147)

See accompanying notes to the consolidated financial statements

## CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended December 31

(millions of dollars)

	2004	2003
<b>Operating activities</b>		
Net income (loss)	42	(491)
Adjust for non-cash items:		
Depreciation and amortization	765	603
Accretion on fixed asset removal and nuclear waste management liabilities	453	430
Earnings on nuclear fixed asset removal and nuclear waste management funds	(313)	(238)
Pension cost (income)	92	(6)
Other post employment benefits and supplementary pension	157	118
Future income taxes (note 11)	(117)	(100)
Provision for restructuring	20	-
Transition rate option contracts	(52)	(43)
Impairment of long-lived assets	-	576
Gain on sale of assets	(3)	-
Gain on sale of investments	-	(58)
Mark-to-market on energy contracts (note 10)	5	(5)
Provision for used nuclear fuel	28	21
Other	29	8
	<b>1,106</b>	<b>815</b>
Contributions to nuclear fixed asset removal and nuclear waste management funds	(454)	(453)
Expenditures on fixed asset removal and nuclear waste management	(71)	(72)
Reimbursement of expenditures on nuclear fixed asset removal and nuclear waste management	19	-
Contributions to pension fund	(154)	(153)
Expenditures on other post employment benefits and supplementary pension	(60)	(56)
Expenditures on restructuring (note 14)	(51)	(68)
Net changes to other long-term assets and liabilities	(26)	(82)
Changes in non-cash working capital balances (note 21)	(83)	166
<b>Cash flow provided by operating activities</b>	<b>226</b>	<b>97</b>
<b>Investing activities</b>		
Sale of accounts receivable	-	300
Proceeds on sale of assets	18	1
Proceeds from sale of investments	-	59
Investment in fixed assets	(561)	(643)
<b>Cash flow (used in) investing activities</b>	<b>(543)</b>	<b>(283)</b>
<b>Financing activities</b>		
Issuance of long-term debt (note 7)	13	51
Repayment of long-term debt (note 7)	(6)	(4)
Dividends paid	-	(17)
Net increase (decrease) in short-term notes (note 6)	26	(182)
<b>Cash flow provided by (used in) financing activities</b>	<b>33</b>	<b>(152)</b>
<b>Net (decrease) in cash and cash equivalents</b>	<b>(284)</b>	<b>(338)</b>
<b>Cash and cash equivalents, beginning of year</b>	<b>286</b>	<b>624</b>
<b>Cash and cash equivalents, end of year</b>	<b>2</b>	<b>286</b>

See accompanying notes to the consolidated financial statements

## CONSOLIDATED BALANCE SHEETS

As at December 31  
(millions of dollars)

	2004	2003
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	2	286
Accounts receivable (note 4)	346	347
Future income taxes (note 11)	44	60
Fuel inventory	569	524
Materials and supplies	92	73
	<b>1,053</b>	1,290
<b>Fixed assets (note 5)</b>		
Property, plant and equipment	15,114	14,701
Less: accumulated depreciation	3,174	2,514
	<b>11,940</b>	12,187
<b>Other long-term assets</b>		
Deferred pension asset (note 9)	524	464
Nuclear fixed asset removal and nuclear waste management funds (note 8)	5,976	5,228
Long-term materials and supplies	281	278
Long-term accounts receivable and other assets	56	64
	<b>6,837</b>	6,034
	<b>19,830</b>	19,511

See accompanying notes to the consolidated financial statements

## CONSOLIDATED BALANCE SHEETS

As at December 31

(millions of dollars)

	2004	2003
<b>Liabilities</b>		
<b>Current liabilities</b>		
Accounts payable and accrued charges (notes 14 and 15)	949	1,064
Market Power Mitigation Agreement rebate payable (note 16)	439	409
Short-term notes payable (note 6)	26	-
Long-term debt due within one year (note 7)	5	4
Deferred revenue due within one year	12	12
Income and capital taxes payable	12	-
	<b>1,443</b>	<b>1,489</b>
<b>Long-term debt (note 7)</b>	<b>3,399</b>	<b>3,393</b>
<b>Other long-term liabilities</b>		
Fixed asset removal and nuclear waste management (note 8)	8,339	7,921
Other post employment benefits and supplementary pension (note 9)	1,105	1,013
Long-term accounts payable and accrued charges	212	276
Deferred revenue	156	168
Future income taxes (note 11)	155	272
	<b>9,967</b>	<b>9,650</b>
<b>Shareholder's equity</b>		
Common shares (note 12)	5,126	5,126
Deficit	(105)	(147)
	<b>5,021</b>	<b>4,979</b>
	<b>19,830</b>	<b>19,511</b>

Commitments and Contingencies (notes 2, 5, 6, 8, 10, 11 and 13)

See accompanying notes to the consolidated financial statements

**On behalf of the Board of Directors:**

**Honourable Jake Epp (signed)**  
Chairman

**James Hankinson (signed)**  
Director

## **NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003**

### **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**

The consolidated financial statements of OPG have been prepared in accordance with Canadian generally accepted accounting principles. The preparation of consolidated 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 Ontario Power Generation Inc. and its subsidiaries. OPG accounts for its interests in jointly controlled entities using the proportionate consolidation method. All significant inter-company transactions have been eliminated on consolidation.

Certain of the 2003 comparative amounts have been reclassified from statements previously presented to conform to the 2004 consolidated 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 \$5 million (2003 – \$21 million) at an average effective rate of 2.2 per cent (2003 - 3.0 per cent) is offset against interest expense in the consolidated statements of income (loss).

#### **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:

Nuclear generating stations	25 and 40 years <sup>1</sup>
Fossil generating stations	40 to 50 years <sup>2</sup>
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	7 years

1 The nuclear stations are depreciated for accounting purposes over 25 years with the exception of Pickering A. The Pickering A station is depreciated over a 40 year operating life as a result of the completion, during the 1980s, of the retubing of the Pickering A station.

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.

## 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 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.

## **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**

In July 2003, OPG and the Province of Ontario (the "Province") completed arrangements pursuant to the Ontario Nuclear Funds Agreement ("ONFA"), which required the establishment of segregated funds to hold the nuclear fixed asset removal and nuclear waste management funds. To comply with the ONFA, OPG transferred the assets in the nuclear fixed asset removal and nuclear waste management funds to the segregated funds called the Decommissioning Fund and the Used Fuel Fund (together the "Funds"). The Funds are invested in debt and equity securities which are treated as long-term investments and are accounted for at amortized cost. The segregated funds are reported as nuclear fixed asset removal and nuclear waste management funds in the consolidated balance sheets. Realized gains and losses on the segregated funds are recorded in earnings in the consolidated statements of income (loss).

With the establishment of the segregated funds accounts in July 2003, the amount receivable from the OEFC was transferred into the Decommissioning Fund in the form of an interest-bearing note and is included in the investments reported in the Decommissioning Fund. Previously, the receivable from the OEFC had been offset against fixed asset removal and nuclear waste management liabilities.

## **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"), formerly known as the Independent Electricity Market Operator ("IMO"). Revenue is recorded as electricity is 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 computes the average spot energy price that prevailed since the beginning of the current settlement period and recognizes a Market Power Mitigation Agreement rebate if the average price exceeds 3.8¢/kilowatt-hour ("kWh"), based on the amount of energy subject to the rebate. 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 (loss). 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 (loss). Accordingly, power purchases of \$170 million in 2004 and \$189 million in 2003 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 an open 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 generation 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 Energy Marketing revenue.

OPG also uses derivative contracts 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.

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.

### **Emission Reduction Credits and Allowances**

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.

### **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 estimates.

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, whereby 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.

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**

OPG operates in two reportable business segments: Generation and Energy Marketing. A separate category, Non-Energy and Other, includes revenue and costs not allocated to the two business segments. Future changes in OPG's structure and operations, including the impact of rate regulation, may change the definition of business segments.

## **Changes in Accounting Policies**

### *Hedging Relationships*

In June 2003, the Accounting Standards Board (“AcSB”) of the Canadian Institute of Chartered Accountants (“CICA”), amended Accounting Guideline 13, *Hedging Relationships*, originally issued in December 2001. This Guideline, effective for fiscal years beginning on or after July 1, 2003, establishes standards for documenting and assessing the effectiveness of hedging activities. OPG adopted the new accounting standard effective January 1, 2004, with no impact on the existing accounting for hedging relationships.

### *Employee Future Benefits - Additional Disclosures*

In December 2003, the AcSB approved revisions to Section 3461, *Employee Future Benefits*. The revisions require additional annual disclosures effective for years ending on or after June 30, 2004, and additional interim disclosure effective for periods ending on or after June 30, 2004. OPG early adopted the interim requirement during the first quarter of 2004, which mandates disclosure of the amount of the total benefit cost. OPG’s 2004 annual disclosure complies with the additional requirements.

## **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 new Financial Accounting Standards Board (“FASB”) 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 (a) 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 (b) 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. The Company assessed these arrangements in advance of the guideline becoming effective January 1, 2005. OPG concluded that the joint venture 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. OPG continues to review its other arrangements.

### *Rate Regulated Accounting*

In December 2004, the *Electricity Restructuring Act, 2004 (Bill 100)* received Royal Assent. A regulation made pursuant to that statute prescribes that OPG’s nuclear and baseload hydroelectric facilities will receive regulated prices for their output. 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. If regulation provides assurance that incurred costs will be recovered in the future, then a regulated entity 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 a regulated entity reports a regulatory liability. Rate regulated assets and liabilities could only be established for OPG after the effective date of a regulation identifying those assets to be regulated.

## **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, the Company 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.

The Company has 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 the year ended December 31, 2004, the Company has recognized pre-tax charges of \$8 million (2003 - \$3 million) on such sales.

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

<i>(millions of dollars)</i>	<b>Principal amount of receivables as at December 31</b>		<b>Average balance of receivables for year ended December 31</b>	
	<b>2004</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>
Total receivables portfolio <sup>1</sup>	<b>490</b>	464	<b>470</b>	443
Receivables sold	<b>300</b>	300	<b>300</b>	300
Receivables retained	<b>190</b>	164	<b>170</b>	143
Average cost of funds			<b>2.6%</b>	2.8%

<sup>1</sup> Amount represents receivables outstanding including receivables that have been securitized since October 1, 2003, 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, 2004 (2003 – nil).

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

<i>(millions of dollars)</i>	<b>2004</b>	<b>2003</b>
Proceeds from new sales	-	300
Collections reinvested in revolving sales <sup>1</sup>	<b>3,600</b>	900
Cash flows from retained interest	<b>2,043</b>	415

<sup>1</sup> 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>	<b>2004</b>	<b>2003</b>
Depreciation and amortization	<b>758</b>	600
Nuclear waste management costs	<b>7</b>	3
	<b>765</b>	603

Fixed assets consist of the following:

<i>(millions of dollars)</i>	<b>2004</b>	<b>2003</b>
Property, plant and equipment		
Nuclear generating stations	<b>4,253</b>	4,087
Fossil-fuelled generating stations	<b>1,591</b>	1,578
Hydroelectric generating stations	<b>7,767</b>	7,659
Other fixed assets	<b>938</b>	636
Construction in progress	<b>565</b>	741
	<b>15,114</b>	14,701
Less: accumulated depreciation		
Generating stations	<b>2,890</b>	2,281
Other fixed assets	<b>284</b>	233
	<b>3,174</b>	2,514
	<b>11,940</b>	12,187

Assets under capital leases of \$203 million (2003 - \$203 million) are included in other fixed assets. Accumulated depreciation on these leased assets at December 31, 2004 was \$53 million (2003 - \$45 million). Interest capitalized to construction in progress at 6.0 per cent (2003 - 6.0 per cent) during the year ended December 31, 2004 was \$30 million (2003 - \$54 million).

### **Impairment of Long-Lived Assets**

The accounting estimates related to asset impairment require significant management judgement to identify factors such as short and long-term forecasts for future sales prices, the supply of electricity in Ontario, the return to service dates of laid-up generating stations, 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.

#### *Coal-Fired Generating Stations*

In 2003, the Government committed to phase out coal-fired generating stations by 2007. As a result, OPG recognized an impairment loss of \$576 million to reflect the termination of cash flows from these stations after 2007, and reduced the carrying amount of the fossil-fuelled generating stations by \$576 million.

The fair value of the coal-fired generating assets was determined using a discounted cash flow method. The fair value determined was then compared to the carrying value of the generating assets in order to determine the amount of the impairment loss.

#### *Lennox Generating Station*

Under the Government "Request for Information/Request for Proposal for 2500 MW of New Clean Generation and Demand Side Management Projects" issued in September 2004, new generators would be allowed to recover fixed costs and an agreed upon rate of return on investment through contractual arrangements. New legislation was passed in December 2004 which provides for the contracted procurement of electricity capacity by the Ontario Power Authority ("OPA"). As a result, new entrants are expected to recover fixed costs through contractual arrangements with the OPA, thereby reducing anticipated prices in the wholesale electricity market as the new entrants will need to recover only fuel and other variable costs from this market. As a relatively high variable cost plant, the Lennox generating station will not be able to recover its fixed and variable costs from the wholesale market in the future. As a result, OPG has entered into discussions with the Province, which it expects will result in an arrangement that will provide for recovery of its fixed and variable costs. If subsequently, a decision is made not to enter into such an agreement, OPG will then be required to record an impairment loss up to the \$205 million carrying value of the generating station, and to assess the possibility of providing for additional losses.

## 6. SHORT-TERM CREDIT FACILITIES

In May 2004, OPG renewed its \$1,000 million revolving, short-term committed bank credit facility with its bank lending group for a further 364-day term. Notes issued under OPG's commercial paper program are supported by the bank credit facility. During 2004, commercial paper of \$1,383 million (2003 - \$965 million) was issued to cover short-term funding requirements, and \$1,357 million (2003 - \$1,147 million) was repaid. As at December 31, 2004, OPG had \$26 million of commercial paper outstanding under this program (2003 - nil). As at December 31, 2004 and 2003, OPG had no other outstanding borrowing under this facility.

OPG also maintains \$26 million (2003 - \$28 million) in short-term uncommitted overdraft facilities as well as \$200 million (2003 - \$173 million) of short-term uncommitted credit facilities, which support the issuance of Letters of Credit. OPG is required to post the Letters of Credit as collateral with Local Distribution Companies ("LDCs") as prescribed by the Ontario Energy Board's ("OEB") Retail Settlement Code, and to support the supplementary pension plan. At December 31, 2004, there were approximately \$155 million (2003 - \$125 million) of Letters of Credit issued for supplementary pension plan and collateral requirements to the LDC's.

## 7. LONG-TERM DEBT

Long-term debt consists of the following:

<i>(millions of dollars)</i>	<b>2004</b>	<b>2003</b>
Notes payable to the OEFC	<b>3,200</b>	3,200
Capital lease obligations	<b>3</b>	8
Share of non-recourse limited partnership debt	<b>201</b>	189
	<b>3,404</b>	3,397
Less: due within one year		
Capital lease obligations	<b>3</b>	4
Share of limited partnership debt	<b>2</b>	-
	<b>5</b>	4
Long-term debt	<b>3,399</b>	3,393

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, 2004 for notes payable to the OEFC are as follows:

Year of Maturity	Interest Rate (%)	Principal Outstanding ( <i>millions of dollars</i> )		Total
		Senior Notes	Subordinated Notes	
2006	5.44	100	-	100
2006	5.62	300	-	300
2006	5.94	100	-	100
2006	5.78	300	-	300
2007	5.85	400	-	400
2008	5.90	400	-	400
2009	6.01	350	-	350
2010	5.49	200	-	200
2010	5.71	300	-	300
2010	6.60	-	375	375
2011	6.65	-	375	375
		2,450	750	3,200

In December 2004, OPG reached an agreement with the OEFC to defer payment on \$500 million principal amount of senior notes maturing in 2005 by extending the maturity dates by five years. The interest rates remain unchanged. This change in maturity dates is reflected in the table above.

In March 2005, the Company reached an agreement with the OEFC to obtain additional financing up to \$600 million.

The Company also reached an agreement with the OEFC to satisfy, via an additional senior note of \$95 million to mature in 2010, its \$95 million interest obligation due in March 2005 related to the debt owing to the OEFC of \$3.2 billion. In addition, the OEFC has agreed that the interest payment of \$98 million due in September 2005 will be satisfied via an additional senior note of \$98 million.

In September 2002, Brighton Beach, a limited partnership formed by OPG, ATCO Power Canada Ltd., ATCO Resources Ltd. and Brighton Beach Power Ltd., completed a \$403 million private bond and term debt financing for its 580-megawatt power project under construction in Windsor, Ontario. Brighton Beach also signed an energy conversion agreement with Coral under which Coral will deliver natural gas to the plant and own, market and trade all the electricity produced. OPG proportionately consolidates its 50 per cent interest in the Brighton Beach partnership. As at December 31, 2004, \$403 million (2003 - \$378 million) was outstanding under the loan and accordingly \$201 million (2003 - \$189 million) was reported by OPG. The project and performance tests were completed in November 2004 and, therefore, any recourse to OPG associated with the above-noted financing of Brighton Beach has been extinguished.

Interest paid during the year ended December 31, 2004 was \$218 million (2003 - \$219 million), of which \$213 million relates to interest paid on long-term debt (2003 - \$210 million).

## 8. 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>	2004	2003
Liability for nuclear used fuel management	4,693	4,451
Liability for nuclear decommissioning and low and intermediate level waste management	3,457	3,289
Liability for non-nuclear fixed asset removal	189	181
Fixed asset removal and nuclear waste management liability	8,339	7,921

The change in the fixed asset removal and nuclear waste management liability for the years ended December 31, 2004 and 2003 is as follows:

<i>(millions of dollars)</i>	2004	2003
Liability, beginning of year	7,921	7,539
Increase in liability due to accretion	453	430
Increase in liability due to nuclear used fuel and nuclear waste management variable expenses	35	24
Fixed asset removal of partnership interests	1	-
Liabilities settled by expenditures on waste management	(71)	(72)
Liability, end of year	8,339	7,921

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 30 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 \$19 billion. The discount rate used to calculate the present value of the liabilities at December 31, 2004 was 5.75 per cent (2003 - 5.75 per cent) and the cost escalation rates ranged from 1 per cent to 4 per cent in 2004 and 2003. 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. 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 are being studied by Canadian nuclear utilities as part of the options study required by the federal *Nuclear Fuel Waste Act* (Canada) ("NFWA"). The options study is to be completed by 2005, with a federal government decision expected no earlier than 2006.

#### *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. 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.

#### *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 2005 and 2034.

In addition to the \$154 million liability for active sites, OPG also has an asset retirement obligation liability of \$35 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 OPG's nuclear fixed asset removal and nuclear waste management liabilities. In July 2003, OPG and the Province completed arrangements, pursuant to the ONFA, which required the establishment of segregated custodial funds to hold the nuclear fixed asset removal and nuclear waste management funds. To comply with the ONFA, OPG transferred

the assets in its existing nuclear fixed asset removal and nuclear waste management funds to a Decommissioning Fund and a Used Fuel Fund, held in segregated custodial accounts. In addition, a receivable due from the OEFC of \$3.1 billion was transferred into the Funds in the form of a \$1.2 billion cash payment and a \$1.9 billion interest-bearing note receivable which is classified as an asset of the Funds and is intended to be funded over the next three years.

The Decommissioning Fund will be used to fund the future costs of nuclear fixed asset removal and long-term low and intermediate level waste management and a portion of used fuel storage costs after station life. The initial funding of the Decommissioning Fund, including the note receivable from the OEFC, is intended to be sufficient to fully discharge the 1999 estimate of the liability. Any shortfall of this fund must be made up by OPG.

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 \$6.0 billion, a present value amount at April 1, 1999 (approximately \$8.3 billion in 2004 dollars) based on used fuel bundle projections consistent with station life included within the financial reference plan. OPG makes quarterly payments over the life of its nuclear generating stations, as specified in the ONFA. Required funding for 2004 under the ONFA was \$454 million, including a contribution of \$100 million to The Ontario NFWA Trust (the "Trust").

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 and contributed \$100 million in each of 2003 and 2004. Under the NFWA, OPG must deposit \$100 million annually into the Trust until the federal government has approved a long-term plan, which is not expected before 2006. Future contributions to the Trust beyond 2005 will be dependent on the direction chosen by the federal government. 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.

The nuclear fixed asset removal and nuclear waste management funds as at December 31, 2004 and 2003 consist of the following:

<i>(millions of dollars)</i>	<b>Amortized Cost Basis</b>		<b>Fair Value</b>	
	<b>2004</b>	2003	<b>2004</b>	2003
Decommissioning Fund	<b>3,858</b>	3,641	<b>4,131</b>	3,801
Used Fuel Fund <sup>1</sup>	<b>2,118</b>	1,587	<b>2,118</b>	1,587
	<b>5,976</b>	5,228	<b>6,249</b>	5,388

<sup>1</sup> The Ontario NFWA Trust represents \$794 million as at December 31, 2004 (2003 - \$648 million) of the Used Fuel Fund on an amortized cost basis.

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 2004 of \$8 million in the first quarter of 2004.

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, 2004, the Used Fuel Fund accounts included an amount due to the Province of \$4 million (2003 – amount due from the Province, \$10 million). If the investments in the Used Fuel Fund were accounted for at fair market value in the consolidated financial statements, at December 31, 2004, there would be an amount due to the Province of \$156 million (2003 – \$71 million).

Under the ONFA, a rate of return target of 5.75 per cent per annum was established for the Decommissioning Fund. 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 under funded. 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, 2004, estimated completion costs under the current approved ONFA Reference Plan are fully funded. The Decommissioning Fund has no excess amount 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, 2004, and the Decommissioning Fund was terminated under the ONFA, there would be an amount due to the Province of \$249 million (2003 - \$128 million).

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, 2004 and 2003 are as follows:

<i>(millions of dollars)</i>	<b>Amortized Cost Basis</b>		<b>Fair Value</b>	
	<b>2004</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>
Cash and cash equivalents and short-term investments	211	139	211	139
Marketable equity securities	3,056	2,556	3,472	2,795
Bonds and debentures	723	635	732	637
Receivable from the OEFC	1,993	1,892	1,993	1,892
Administrative expense payable	(3)	(4)	(3)	(4)
	<b>5,980</b>	5,218	<b>6,405</b>	5,459
Due (to) from Province – Used Fuel Fund	(4)	10	(156)	(71)
<b>Total</b>	<b>5,976</b>	5,228	<b>6,249</b>	5,388

The bonds and debentures held in the Used Fuel Fund and the Decommissioning Fund as at December 31, 2004 and 2003 mature according to the following schedule:

<i>(millions of dollars)</i>	Fair Value	
	2004	2003
Less than 1 year	-	19
1 - 5 years	259	204
5 - 10 years	233	260
More than 10 years	240	154
Total maturities of debt securities	732	637
Average yield	4.1%	4.3%

The receivable of \$1,993 million (2003 - \$1,892 million) from the OEFC does not have a specified maturity date. The effective rate of interest on the OEFC receivable was 5.3 per cent in 2004 (2003 - 5.0 per cent since commencement of the ONFA in July 2003).

## 9. 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 all regular 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 plan is a defined benefit plan 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, 2004.

	Registered and Supplementary Pension Plans		Other Post Employment Benefits	
	2004	2003	2004	2003
Weighted Average Assumptions – Benefit Obligation at Year End				
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%

	Registered and Supplementary Pension Plans		Other Post Employment Benefits	
	2004	2003	2004	2003
Weighted Average Assumptions – Cost for the Year				
Expected return on plan assets net of expenses	7.00%	7.00%		
Rate used to discount future benefits	6.25%	6.75%	6.17%	6.60%
Salary schedule escalation rate	3.25%	3.00%	-	-
Rate of cost of living increase to pensions	2.25%	2.00%	-	-
Initial health care trend rate	-	-	6.33%	6.42%
Ultimate health care trend rate	-	-	4.46%	4.13%
Year ultimate rate reached	-	-	2010	2010
Rate of increase in disability benefits	-	-	2.25%	2.00%
Average remaining service life for employees (years)	12	12	12	11

	Registered Pension Plan		Supplementary Pension Plan		Other Post Employment Benefits	
	2004	2003	2004	2003	2004	2003
<i>(millions of dollars)</i>						
Changes in Plan Assets						
Fair value of plan assets at beginning of year	6,449	5,727	-	-	-	-
Contributions by employer	154	153	6	5	54	51
Contributions by employees	52	52	-	-	-	-
Actual return on plan assets net of expenses	693	783	-	-	-	-
Settlements	(4)	-	-	-	-	-
Benefit payments	(288)	(266)	(6)	(5)	(54)	(51)
Fair value of plan assets at end of year	7,056	6,449	-	-	-	-
Changes in Projected Benefit Obligation						
Projected benefit obligation at beginning of year	7,046	5,965	117	125	1,307	1,079
Employer current service costs	143	107	8	8	41	29
Contributions by employees	52	52	-	-	-	-
Interest on projected benefit obligation	442	402	7	9	82	64
Curtailment loss (gain)	2	-	-	-	(1)	-
Settlement gain	(4)	-	-	-	-	-
Benefit payments	(288)	(266)	(6)	(5)	(54)	(51)
Net actuarial loss (gain)	270	786	18	(20)	124	186
Projected benefit obligation at end of year	7,663	7,046	144	117	1,499	1,307
Funded Status – Surplus (Deficit) at end of year	(607)	(597)	(144)	(117)	(1,499)	(1,307)

	<b>2004</b>	<b>2003</b>
Registered pension plan fund asset investment categories		
Equities	<b>65%</b>	65%
Fixed income	<b>33%</b>	34%
Cash and short-term	<b>2%</b>	1%
<b>Total</b>	<b>100%</b>	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.

The most recently filed funding valuation was done as at April 1, 2002. Using a going-concern funding basis, with assets at market value, OPG estimates that there was a pension fund deficit of \$1.5 billion at December 31, 2004 (2003 - \$1.3 billion deficit). The deficit disclosed in the next filed funding valuation, which must have an effective date of no later than April 1, 2005, could be significantly different.

The supplementary plan is not funded, but is secured by letters of credit totalling \$125 million.

	<b>Registered Pension Plan</b>		<b>Supplementary Pension Plan</b>		<b>Other Post Employment Benefits</b>	
	<b>2004</b>	2003	<b>2004</b>	2003	<b>2004</b>	2003
<i>(millions of dollars)</i>						
Reconciliation of Funded Status to Accrued Benefit Asset (Liability)						
Funded status – surplus (deficit) at end of year	<b>(607)</b>	(597)	<b>(144)</b>	(117)	<b>(1,499)</b>	(1,307)
Unamortized net actuarial loss	<b>1,012</b>	924	<b>28</b>	10	<b>422</b>	313
Unamortized past service costs	<b>119</b>	137	<b>5</b>	6	<b>18</b>	21
Accrued benefit asset (liability) at end of year	<b>524</b>	464	<b>(111)</b>	(101)	<b>(1,059)</b>	(973)
Short-term portion	-	-	<b>(6)</b>	(3)	<b>(59)</b>	(58)
Long-term portion	<b>524</b>	464	<b>(105)</b>	(98)	<b>(1,000)</b>	(915)

	<b>Registered Pension Plan</b>		<b>Supplementary Pension Plan</b>		<b>Other Post Employment Benefits</b>	
	<b>2004</b>	2003	<b>2004</b>	2003	<b>2004</b>	2003
<i>(millions of dollars)</i>						
Components of Cost Recognized						
Current service costs	<b>143</b>	107	<b>8</b>	8	<b>41</b>	29
Interest on projected benefit obligation	<b>442</b>	402	<b>7</b>	9	<b>82</b>	64
Expected return on plan assets net of expenses	<b>(511)</b>	(502)	-	-	-	-
Curtailment loss (gain)	<b>2</b>	-	-	-	<b>(1)</b>	-
Amortization of past service costs	<b>18</b>	18	<b>1</b>	1	<b>3</b>	3
Amortization of net actuarial (gain) loss	-	(31)	-	2	<b>15</b>	2
<b>Cost (income) recognized</b>	<b>94</b>	(6)	<b>16</b>	20	<b>140</b>	98

	Registered Pension Plan		Supplementary Pension Plan		Other Post Employment Benefits	
<i>(millions of dollars)</i>	2004	2003	2004	2003	2004	2003
Components of Cost Incurred and Recognized						
Current service costs	143	107	8	8	41	29
Interest on projected benefit obligation	442	402	7	9	82	64
Actual return on plan assets net of expenses	(693)	(783)	-	-	-	-
Curtailment loss (gain)	2	-	-	-	(1)	-
Net actuarial loss (gain)	270	786	18	(20)	124	186
Cost incurred in year	164	512	33	(3)	246	279
Differences between costs incurred and recognized in respect of:						
Actual return on plan assets net of expenses	182	281	-	-	-	-
Past service costs	18	18	1	1	3	3
Net actuarial (gain) loss	(270)	(817)	(18)	22	(109)	(184)
Cost (income) recognized	94	(6)	16	20	140	98

A 1.0 per cent increase or decrease in the health care trend rate would result in an increase in the service and interest components of the 2004 OPEB cost recognized of \$21 million (2003 - \$14 million) or a decrease in the service and interest components of the 2004 OPEB cost recognized of \$19 million (2003 - \$11 million), respectively. A 1.0 per cent increase or decrease in the health care trend rate would result in an increase in the projected OPEB obligation at December 31, 2004 of \$221 million (2003 - \$169 million) or a decrease in the projected OPEB obligation at December 31, 2004 of \$175 million (2003 - \$152 million).

## 10. 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 decreased Energy Marketing revenue by \$2 million during 2004 (2003 – increased 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 Energy Marketing 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>	<b>Notional Quantity</b>	<b>Terms</b>	<b>Fair Value</b>	<b>Notional Quantity</b>	<b>Terms</b>	<b>Fair Value</b>
		<b>2004</b>			<b>2003</b>	
(Loss)/gain						
Electricity derivative instruments	<b>10.4 TWh</b>	<b>1-3 yrs</b>	<b>(71)</b>	23.9 TWh	1-3 yrs	(13)
Foreign exchange derivative instruments	<b>US \$10</b>	<b>Jan/05</b>	-	US \$40	Jan/04	(3)
Option to purchase emission reduction credits	-	-	-	3,000,000 tonnes	2004	-

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, 2004 was US \$0.81 (2003 – US \$0.72) 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>	<b>Notional Quantity</b>	<b>Fair Value</b>	<b>Notional Quantity</b>	<b>Fair Value</b>
	<b>2004</b>		<b>2003</b>	
Commodity derivative instruments				
Assets	<b>7.9 TWh</b>	<b>12</b>	7.9 TWh	8
Liabilities	<b>1.3 TWh</b>	<b>(12)</b>	1.6 TWh	(8)
Ontario market liquidity reserve		<b>(7)</b>		(5)
Total		<b>(7)</b>		(5)

### 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 2004	Fair Value	Carrying Value 2003	Fair Value
Financial Assets				
Nuclear fixed asset removal and nuclear waste management funds	5,976	6,249	5,228	5,388
Long-term accounts receivable and other assets	56	56	64	64
Financial Liabilities				
Long-term debt	3,399	3,577	3,393	3,516
Long-term accounts payable and accrued charges	212	212	276	276

### Credit Risk

The majority of OPG's revenues are derived from electricity sales through the IESO administered spot market. OPG also derives revenue from several other sources including the sale of financial risk management products to third parties. OPG manages counterparty credit risk by monitoring and limiting its exposure to counterparties with lower credit ratings, evaluating its counterparty credit exposure on an integrated basis, and by performing periodic reviews of the credit worthiness of all counterparties, including obtaining credit security for all transactions beyond approved limits.

### 11. INCOME TAXES

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

<i>(millions of dollars)</i>	2004	2003
(Loss) before income taxes	(38)	(494)
Combined Canadian federal and provincial statutory income tax rates, including surtax	36.1%	36.6%
Statutory income tax rates applied to accounting income	(14)	(181)
Increase (decrease) in income taxes resulting from:		
Large corporations tax in excess of surtax	30	37
Lower future tax rate on temporary differences	(3)	4
Non-taxable income items	(4)	(3)
Adjustment for changes in future income tax rates	-	30
Valuation allowance	(93)	93
Other	4	17
	(66)	178
Recovery of income taxes	(80)	(3)
Effective rate of income taxes	210.5%	0.6%

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

<i>(millions of dollars)</i>	<b>2004</b>	<b>2003</b>
Current income tax expense	<b>21</b>	80
Future income tax expense (benefits):		
Change in temporary differences	<b>50</b>	(64)
Non-capital loss carry-forward	<b>(67)</b>	(101)
Future recoverable Ontario minimum tax	-	(41)
Valuation allowance (reversal)	<b>(93)</b>	93
Adjustment for changes in future income tax rates	-	30
Other	<b>9</b>	-
<b>Income tax recoveries</b>	<b>(80)</b>	<b>(3)</b>

At December 31, 2004, OPG had approximately \$493 million (2003 – \$296 million) of non-capital loss carry-forwards for which the Company recognized future tax assets of \$67 million in 2004 and \$101 million in 2003 for financial reporting purposes. The 2003 loss will expire in 2010 and the 2004 loss will expire in 2014.

The amount of cash income taxes paid in the year ended December 31, 2004 was \$17 million (2003 - \$28 million). OPG reported nil in other current income tax amounts recoverable (2003 - \$16 million).

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>	<b>2004</b>	<b>2003</b>
Future income tax assets:		
Fixed asset removal and nuclear waste management liabilities	<b>2,806</b>	2,664
Other liabilities and assets	<b>446</b>	443
Non-capital loss carry-forward	<b>168</b>	101
Future recoverable Ontario minimum tax	<b>42</b>	41
	<b>3,462</b>	3,249
Future income tax liabilities:		
Fixed assets	<b>1,211</b>	1,422
Fixed asset removal and nuclear waste management fund	<b>2,039</b>	1,784
Other liabilities and assets	<b>323</b>	255
	<b>3,573</b>	3,461
Net future income tax liabilities	<b>111</b>	212
Represented by:		
Current portion	<b>(44)</b>	(60)
Long-term portion	<b>155</b>	272
	<b>111</b>	212

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. Accordingly, there is uncertainty around the amount of the tax provision and management is not able to determine the impact on the consolidated financial statements.

## **12. COMMON SHARES**

As at December 31, 2004 and 2003, 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. Dividends are declared and paid to achieve an effective 35 per cent pay-out based on annual net income.

## **13. COMMITMENTS AND CONTINGENCIES**

### **Litigation**

Various lawsuits are pending against OPG or its subsidiaries covering a wide range of matters that arise in the ordinary course of its business activities. Each of these matters is subject to various uncertainties. Some of these matters may be resolved unfavourably with respect to OPG. These contingencies are provided for when they are likely to occur and are reasonably estimable. Management believes that the ultimate resolution of these matters will not have a material effect on OPG's financial position.

In July 2004, OPG was charged with criminal negligence causing death and criminal negligence causing bodily harm in relation to the 2002 accident at Barrett Chute. These charges are still pending and OPG has some reasonable defences. However, regardless of whether OPG is convicted of these charges, OPG does not anticipate a material adverse effect on OPG's financial position.

### **Aboriginal Claims and Litigation**

The Slate Falls First Nation claim is for \$40 million. The First Nation has commenced an action in the Ontario Court for declaratory relief and unspecified damages for interference with reserve and traditional land rights from flooding and other acts of trespass. The Government of Canada is also a defendant to this claim. The First Nation is composed of former members of a number of different bands including Osnaburgh. Ontario Hydro had previously entered into a settlement agreement with the Mishkeegogamang First Nation, which was previously known as the Osnaburgh First Nation. Both the Government of Canada and OPG are considering the potential overlap of beneficiaries between the present litigation and the prior settlement. The parties are in the preliminary stage of gathering documentary evidence to assist in the assessment of liability and potential damages, and therefore, are unable to evaluate the claim at this time.

Preliminary motions have been resolved in favour of Slate Falls First Nation. As a result, a member of the Slate Falls First Nation has been granted status to represent some 200 living and dead aboriginal people who are or were members of the Slate Falls First Nation. OPG and Canada's motion for summary judgment dismissing the plaintiff's action was dismissed. All appeals are now complete and Canada is seeking to add the Province of Ontario and Mishkeegogamang as parties. Canada is being separately sued by Mishkeegogamang and is seeking to have OPG and Ontario added as parties to this proceeding. Any monies OPG would have to pay to Canada by way of indemnity in this action would, under the terms of the settlement it reached with Mishkeegogamang, be credited against the monies OPG owes under the settlement.

The Whitesand and Red Rock First Nations have commenced a claim for damages in an unspecified amount for interference with reserve and traditional land rights in the Nipigon River Basin, north of Thunder Bay, from flooding and other acts of trespass. The federal and provincial Crowns and Hydro One are also defendants.

### **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, 2004, expenditures of \$2 million (2003 - \$4 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, stand-by Letters of Credit and surety bonds.

OPG has provided limited guarantees in connection with its share of the Brighton Beach financing, whereby it is responsible for contributing its share of equity related to cost overruns associated with the construction of the generating station. As at December 31, 2004, OPG remains responsible for contributing its share of equity related to cost overruns, up to \$6 million. As Brighton Beach commenced commercial operation in July 2004, any cost overruns are now primarily limited to settlement of construction liens registered by some contractors associated with the construction project. The maximum potential future payments are unknown because Brighton Beach has yet to complete its review and resolution of existing liens. Brighton Beach is currently negotiating settlement of these liens.

### Contractual Commitments

The Company's contractual obligations and other commercial commitments as at December 31, 2004 are as follows:

<i>(millions of dollars)</i>	2005	2006	2007	2008	2009	Thereafter	Total
Fuel supply agreements	526	386	203	120	36	34	1,305
Contributions under ONFA	454	454	454	679	350	1,753	4,144
Long-term debt repayment	-	800	400	400	350	1,345	3,295
Interest on long-term debt	99	191	145	122	99	86	742
Unconditional purchase obligations	39	27	16	12	14	50	158
Long-term accounts payable	28	28	28	10	-	-	94
Operating lease obligations	7	5	4	4	-	19	39
Other	76	35	36	37	37	25	246
<b>Total</b>	<b>1,229</b>	<b>1,926</b>	<b>1,286</b>	<b>1,384</b>	<b>886</b>	<b>3,312</b>	<b>10,023</b>

### 14. RESTRUCTURING

The change in the restructuring liability for termination benefits for the years ended December 31, 2004 and 2003 is as follows:

<i>(millions of dollars)</i>	2004	2003
Liability, beginning of year	52	120
Restructuring charges	19	-
Payments	(51)	(68)
<b>Liability, end of year</b>	<b>20</b>	<b>52</b>

OPG recorded restructuring charges of \$16 million, which consisted of \$15 million for termination benefits and \$1 million in related pension and other post employment benefits expenses associated with its

Lakeview generating station during the second quarter of 2004. OPG is required by regulation to cease burning coal at its Lakeview generating station by the end of April 2005. OPG has communicated its plan to shut down the Lakeview generating station to all employees. As at December 31, 2004, 81 employees had accepted the termination package offered. OPG also recorded restructuring charges of \$4 million related to its Energy Marketing segment.

#### **15. TRANSITION RATE OPTION CONTRACTS**

Under regulation known as Transition - Generation Corporation Designated Rate Options ("TRO"), OPG is required to provide transitional price relief upon 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 is approximately 5.4 TWh in the first year after market opening, 3.6 TWh in the second year and 1.8 TWh in each of the third and fourth years. The maximum length of the program is four years.

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. OPG no longer expects to meet the decontrol targets necessary for TRO contracts to expire after three years. As a result, an additional charge of \$30 million related to the fourth year of the TRO contracts was recorded in 2003.

During 2004, \$52 million (2003 - \$73 million) was charged against the provision and included in Generation revenue.

#### **16. MARKET POWER MITIGATION AGREEMENT REBATE**

Until April 1, 2005, OPG is 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 include both a rebate mechanism and the requirement to decontrol generating capacity. Under the rebate mechanism, a significant majority of OPG's expected energy sales in Ontario are subject to an average annual revenue cap of 3.8¢/kWh. During the term of the MPMA, OPG is required to pay a rebate to the IESO 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 is being replaced effective April 1, 2005, by a regulated price for baseload hydroelectric and nuclear generation. In addition, eighty-five per cent of unregulated OPG electricity generation, excluding generation from the Lennox generating station and volumes relating to existing contracts will be subject to a revenue limit based on an average price of 4.7¢/kWh. This revenue limit will be in place for a period of 13 months.

In accordance with the Market Power Mitigation Agreement, the rebate is 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 2004 average hourly spot price exceeded the 3.8¢/kWh revenue cap, OPG provided \$1,154 million (2003 - \$1,510 million) as a Market Power Mitigation Agreement rebate.

The change in the Market Power Mitigation Agreement rebate liability for the years ended December 31, 2004 and 2003 were as follows:

<i>(millions of dollars)</i>	<b>2004</b>	<b>2003</b>
Liability, beginning of year	<b>409</b>	572
Increase to provision during the year	<b>1,154</b>	1,510
Payments	<b>(1,124)</b>	(1,673)
Liability, end of year	<b>439</b>	409

## **17. RESEARCH AND DEVELOPMENT**

For the year ended December 31, 2004, \$21 million (2003 - \$21 million) of research and development expenses were charged to operations.

## **18. BUSINESS SEGMENTS**

### **Description of Reportable Segments**

With the opening of Ontario's electricity market to competition on May 1, 2002, OPG began operating two reportable business segments: Generation and Energy Marketing. A separate category, Non-Energy and Other, includes revenue and certain costs which are not allocated to the business segments.

### **Generation Segment**

OPG's principal business segment operates in Ontario, generating and selling electricity. Commencing with the opening of the Ontario electricity market on May 1, 2002, all of OPG's electricity generation is sold into the IESO-administered real-time energy spot market. As such, the majority of OPG's revenue is derived from spot market sales. In addition to revenue earned from spot market sales, revenue is also earned through offering available 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.

### **Energy Marketing Segment**

The Energy Marketing segment derives revenues from various financial and physical energy market transactions with large and medium volume end-use customers and intermediaries such as utilities, brokers, aggregators, traders and other power marketers and retailers. Energy marketing in deregulated markets includes trading, the sale of financial risk management products and sales of energy-related products and services to meet customers' needs for energy solutions. All contracts that are not designated as hedges are recorded as assets or liabilities at fair value, with changes in fair value recorded in Energy Marketing revenue as gains or losses. OPG purchases and sells electricity through the IESO market and the interconnected markets of other provinces and the U.S. northeast and midwest.

### **Non-Energy and Other**

OPG derives Non-Energy revenue under the terms of its long-term lease arrangement with Bruce Power related to the Bruce nuclear generating stations. This includes lease revenue, interest income and revenue from engineering analysis and design, technical and ancillary services. Non-energy revenue also includes isotope sales to the medical industry and real estate rentals.

### 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. As part of the initial payment, OPG received \$370 million in cash proceeds and a \$225 million note receivable, which was repaid in 2003.

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 payment 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 Non-Energy 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. In addition, for 2004 through 2008, minimum payments under the lease are \$190 million annually, subject to limited exceptions. The lease revenue of \$236 million (2003 - \$189 million) was recorded in Non-Energy revenue. The remaining terms of the operating lease agreement remain substantially unchanged.

The net book value of fixed assets on lease to Bruce Power at December 31, 2004, was \$590 million (2003 - \$680 million).

<b>Segment Income for year ended December 31, 2004</b>	<b>Generation</b>	<b>Energy Marketing</b>	<b>Non-Energy and Other</b>	<b>Total</b>
<i>(millions of dollars)</i>				
Revenues				
Revenue before Market Power Mitigation Agreement rebate	5,637	47	388	6,072
Market Power Mitigation Agreement rebate	(1,154)	-	-	(1,154)
	4,483	47	388	4,918
Fuel expense	1,153	-	-	1,153
Gross margin	3,330	47	388	3,765
Operations, maintenance and administration excluding Pickering A return to service	2,259	6	58	2,323
Pickering A return to service	271	-	-	271
Depreciation and amortization	669	-	96	765
Accretion on fixed asset removal and nuclear waste management liabilities	453	-	-	453
Earnings on nuclear fixed asset removal and nuclear waste management funds	(313)	-	-	(313)
Property and capital taxes	88	-	15	103
(Loss) income before the following:	(97)	41	219	163
Restructuring	20	-	-	20
Other income	-	-	(8)	(8)
Net interest expense	-	-	189	189
(Loss) income before income taxes	(117)	41	38	(38)

<b>Segment Income for year ended December 31, 2003</b>	<b>Generation</b>	<b>Energy Marketing</b>	<b>Non-Energy and Other</b>	<b>Total</b>
<i>(millions of dollars)</i>				
Revenues				
Revenue before Market Power Mitigation Agreement rebate	6,300	68	320	6,688
Market Power Mitigation Agreement rebate	(1,510)	-	-	(1,510)
	4,790	68	320	5,178
Fuel expense	1,678	-	-	1,678
Gross margin	3,112	68	320	3,500
Operations, maintenance and administration excluding Pickering A return to service	2,072	8	55	2,135
Pickering A return to service	258	-	-	258
Depreciation and amortization	496	-	107	603
Accretion on fixed asset removal and nuclear waste management liabilities	430	-	-	430
Earnings on nuclear fixed asset removal and nuclear waste management funds	(238)	-	-	(238)
Property and capital taxes	98	-	16	114
Loss on transition rate option contracts	-	-	30	30
(Loss) income before the following:	(4)	60	112	168
Impairment of long-lived assets	576	-	-	576
Other income	-	-	(58)	(58)
Net interest expense	-	-	144	144
(Loss) income before income taxes	(580)	60	26	(494)

<b>Selected Balance Sheet Information</b>	<b>Generation</b>	<b>Energy Marketing</b>	<b>Non-Energy and Other</b>	<b>Total</b>
<i>(millions of dollars)</i>				
December 31, 2004				
Segment property, plant and equipment, net	11,065	-	875	11,940
December 31, 2003				
Segment property, plant and equipment, net	11,252	-	935	12,187

<b>Selected Cash Flow Information</b>				
<i>(millions of dollars)</i>				
Year ended December 31, 2004				
Capital expenditures	513	-	48	561
Year ended December 31, 2003				
Capital expenditures	546	-	97	643

Substantially all sales were in Canada. All of OPG's electricity generation was sold into the real-time energy spot market administered by the IESO. As such, the majority of OPG's revenue was derived from spot market sales. Sales to the IESO represented 91 per cent of total revenues for the year ended December 31, 2004 (2003 - 93 per cent) and 47 per cent of accounts receivable as at December 31, 2004 (2003 - 40 per cent).

## 19. 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>	<b>Revenues</b>	<b>Expenses</b>	<b>Revenues</b>	<b>Expenses</b>
	<b>2004</b>		<b>2003</b>	
Hydro One				
Electricity sales	<b>40</b>	-	36	-
Services	-	<b>12</b>	14	16
Settlement Transactions	-	<b>33</b>	-	36
Province of Ontario				
GRC water rentals and land tax	-	<b>152</b>	-	132
Guarantee fee	-	<b>8</b>	-	3
Used Fuel Fund rate of return guarantee	-	<b>14</b>	-	(10)
Other	-	<b>2</b>	-	-
OEFC				
GRC and proxy property tax	-	<b>214</b>	-	205
Interest income on receivable	-	<b>(101)</b>	-	(155)
Interest expense on long-term notes	-	<b>191</b>	-	191
Capital tax	-	<b>49</b>	-	51
Income taxes	-	<b>(80)</b>	-	(3)
Indemnity fees	-	<b>5</b>	-	5
IESO				
Electricity sales	<b>5,465</b>	<b>304</b>	6,212	331
Market Power Mitigation Agreement rebate	<b>(1,154)</b>	-	(1,510)	-
Ancillary services	<b>90</b>	-	77	-
Other	<b>1</b>	<b>1</b>	1	1
	<b>4,442</b>	<b>804</b>	4,830	803

At December 31, 2004, accounts receivable included \$14 million (2003 - \$14 million) due from Hydro One and \$158 million (2003 - \$134 million) due from the IESO. Accounts payable and accrued charges at December 31, 2004 included \$3 million (2003 - \$5 million) due to Hydro One.

## 20. OTHER INCOME

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. In 2003, other income of \$58 million was from the gain on sale of long-term investments.

**21. CHANGES IN NON-CASH WORKING CAPITAL BALANCES**

<i>(millions of dollars)</i>	<b>2004</b>	<b>2003</b>
Accounts receivable	<b>(15)</b>	105
Note receivable	-	225
Income taxes recoverable	<b>16</b>	64
Future income tax asset	<b>16</b>	17
Fuel inventory	<b>(45)</b>	(10)
Materials and supplies	<b>(19)</b>	-
Market Power Mitigation Agreement rebate payable	<b>30</b>	(163)
Accounts payable and accrued charges	<b>(78)</b>	(72)
Income and capital taxes payable	<b>12</b>	-
	<b>(83)</b>	166