

FINANCIAL STATEMENTS OF
TAY HYDRO ELECTRIC
DISTRIBUTION COMPANY INC.

December 31, 2006

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AUDITORS' REPORT

To the Shareholders of
Tay Hydro Electric Distribution Company Inc.

We have audited the balance sheet of Tay Hydro Electric Distribution Company Inc. as at December 31, 2006 and the statements of retained earnings, income and cash flows for the year then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, these financial statements present fairly, in all material respects, the financial position of the company as at December 31, 2006 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

The financial statements as at December 31, 2005 and for the year then ended were audited by other auditors who expressed an opinion without reservation on those statements in their report dated April 7, 2006.

Collins Barrow Kawarthas

Chartered Accountants
Licensed Public Accountants

Peterborough, Ontario
June 15, 2007

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.
BALANCE SHEET

As at December 31, 2006

	2006	2005
	\$	\$
ASSETS		
Current assets		
Cash	1,131,051	1,474,591
Accounts receivable	378,867	294,146
Income taxes receivable	-	139,696
Inventory	119,042	104,857
Prepaid expenses	46,109	25,638
Due from related parties (note 3)	84,878	61,012
Unbilled revenue	622,622	580,530
	<u>2,382,569</u>	<u>2,680,470</u>
Other assets		
Property, plant and equipment (note 4)	2,814,651	2,732,653
Regulatory assets (note 6)	97,789	386,323
Other assets (note 5)	16,567	166,247
	<u>2,929,007</u>	<u>3,285,223</u>
	<u>5,311,576</u>	<u>5,965,693</u>

The accompanying notes are an integral part of these financial statements

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.

BALANCE SHEET

As at December 31, 2006

	2006 \$	2005 \$
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued liabilities	855,346	1,091,346
Income taxes payable	141,010	-
Current portion of long-term debt (note 7)	1,952,821	1,939,821
	<u>2,949,177</u>	<u>3,031,167</u>
Long-term liabilities		
Long-term debt (note 7)	422,200	633,000
Customer and retailer deposits	139,132	116,367
Development charges (note 9)	-	118,678
Regulatory liabilities (note 6)	30,021	59,397
	<u>591,353</u>	<u>927,442</u>
Shareholders' equity		
Share capital (note 8)	1,742,821	1,742,821
Retained earnings	28,225	264,263
	<u>1,771,046</u>	<u>2,007,084</u>
	<u>5,311,576</u>	<u>5,965,693</u>

Approved on behalf of the Board

Director

Director

The accompanying notes are an integral part of these financial statements

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.

STATEMENT OF RETAINED EARNINGS

For the year ended December 31, 2006

	2006 \$	2005 \$
Retained earnings - beginning of year		
As previously stated	264,263	135,657
<u>Equity adjustment (note 9)</u>	<u>118,678</u>	<u>-</u>
As restated	382,941	135,657
Net income (loss) for the year	(33,716)	128,606
<u>Dividends paid</u>	<u>(321,000)</u>	<u>-</u>
Retained earnings - end of year	28,225	264,263

The accompanying notes are an integral part of these financial statements

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.

STATEMENT OF INCOME

For the year ended December 31, 2006

	2006 \$	2005 \$
Revenue		
Sale of power	3,314,322	3,218,878
Distribution	1,203,145	1,323,182
	4,517,467	4,542,060
Cost of sales		
Power purchased	3,314,322	3,218,878
Gross profit	1,203,145	1,323,182
Expenses		
Distribution	198,184	210,836
Amortization	282,724	278,586
Operations and administration	309,680	528,017
Billing and collecting	222,770	221,416
	1,013,358	1,238,855
Income before undernoted items and income taxes	189,787	84,327
Other income (expense)		
Interest income	70,013	35,225
Other income	101,842	109,512
Interest on long term debt	(169,861)	(181,158)
	1,994	(36,421)
Income before income taxes	191,781	47,906
Provision for (recovery of) income taxes	225,497	(80,700)
Net income (loss) for the year	(33,716)	128,606

The accompanying notes are an integral part of these financial statements

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.
STATEMENT OF CASH FLOWS

For the year ended December 31, 2006

	2006 \$	2005 \$
CASH PROVIDED FROM (USED FOR)		
Operating activities		
Net income (loss) for the year	(33,716)	128,606
Items not affecting cash		
Amortization	282,724	278,586
	249,008	407,192
Change in non-cash working capital items (note 10)	(117,864)	287,350
	131,144	694,542
Investing activities		
Purchase of property, plant and equipment	(359,200)	(105,352)
Decrease (increase) in regulatory liabilities	(29,376)	14,383
Decrease (increase) in other assets	144,158	(25,912)
Decrease (increase) in regulatory assets	288,534	181,156
	44,116	64,275
Financing activities		
Dividends paid	(321,000)	-
Repayment of long-term debt	(197,800)	(186,000)
	(518,800)	(186,000)
Increase (decrease) in cash	(343,540)	572,817
Cash - beginning of year	1,474,591	901,774
Cash - end of year	1,131,051	1,474,591

The accompanying notes are an integral part of these financial statements

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2006

1. NATURE OF OPERATIONS

Tay Hydro Electric Distribution Company Inc. is incorporated under the Business Corporations Act of the Province of Ontario.

The principal activity of the company is to distribute electricity to the residents and businesses in the Township of Tay under license issued by the Ontario Energy Board (OEB). The company is regulated by the OEB and adjustments to its distribution rates require OEB approval.

2. SIGNIFICANT ACCOUNTING POLICIES

These financial statements are prepared in accordance with Canadian generally accepted accounting principles. The significant policies are detailed as follows:

(a) *Electricity Regulation*

The company is subject to rate regulation by the Ontario Energy Board (OEB). The OEB is charged with the responsibility of approving rates for the transmission and distribution of electricity. The following regulatory policies are practiced in a rate regulated environment.

(i) Regulatory Assets

Regulatory assets consist of deferred qualifying transition costs and various rate and retail variance accounts. The costs related to these accounts are deferred for accounting purposes because it is probable that they will be recovered in future rates. Regulatory assets recognized at December 31, 2006 are disclosed in Note 6. The company continually assesses to the likelihood of the recovery of these assets. If recovery is no longer considered probable, the amount are charged to operations in the year the assessment is made. The recovery of regulatory assets commenced April 1, 2004.

(ii) Corporate Taxes

Under the Electricity Act, 1998, the company is required to make payments in lieu of income taxes (PILS) to the Ontario Electricity Financial Corporation (OEFC). As directed by the OEB, the company provides for PILS payments using the taxes payable method. Under the taxes payable method, no provisions are made for future income taxes as a result of temporary differences between the tax basis of assets and liabilities and their carrying amounts.

(b) *Inventory*

Inventory is valued at the lower of cost and net realizable value with costs being determined on a weighted average basis. Inventory consists primarily of repair parts, supplies and materials held for future capital expansion.

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2006

2. SIGNIFICANT ACCOUNTING POLICIES, continued

(c) Revenue recognition

Revenues are recorded on the basis of regular meter readings and estimated customer usage since the last meter reading date to the end of the period. The related cost of power is recorded on the basis of the power billed by Hydro One.

(d) Property, plant and equipment

Property, plant and equipment are recorded at cost. The company provides for amortization using the straight-line method at rates designed to amortize the cost of the property, plant and equipment over their estimated useful lives. The annual amortization rates are as follows:

Buildings	25-30 years
Distribution system	25 years
Land rights	50 years
Other capital assets	2-10 years

(e) Asset retirement obligations

Canadian generally accepted accounting principles require the company to determine the fair value of the future expenditures required to settle legal obligations to remove fixed assets on retirement. If reasonably estimable, a liability is recognized equal to the present value of the estimated future removal expenditures.

Some of the company's assets may have asset retirement obligations. As the company expects to use the majority of its fixed assets for an indefinite period, no removal costs can be determined and, consequently, a reasonable estimate of the fair value of any asset retirement obligations has not been made at this time.

(f) Financial instruments

The company's financial instruments consist of cash, accounts receivable, unbilled revenue, due from related parties, accounts payable and accrued liabilities and long-term debt. Unless otherwise noted it is management's opinion that the company is not exposed to significant interest, currency or credit risks arising from these financial instruments. The fair values of these financial instruments approximate their carrying values, unless otherwise noted.

(g) Management estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2006

2. SIGNIFICANT ACCOUNTING POLICIES, continued

(h) Prior year's figures

Prior year's figures have been restated, where applicable, to conform to current year's presentation.

3. RELATED PARTY TRANSACTIONS

(a) During the year, the company entered into transactions with the following related parties:

Tay Utility Contracting Inc., related company
Township of Tay, shareholder of parent company

(b) Transactions

	2006 \$	2005 \$
Revenue		
Services - Tay Utility Contracting Inc.	18,825	9,104
Sale of Power - Township of Tay	305,064	277,087
	323,889	286,191
Expenses		
Interest expense - Township of Tay	169,861	182,058
Property taxes - Township of Tay	14,435	13,418
	184,296	195,476

These transactions are in the normal course of operations and have been valued in these financial statements at the exchange amount which is the amount of consideration established and agreed to by the related parties.

The advances are non-interest bearing with no set terms of repayment.

(c) The amounts due from related companies consists of:

	2006 \$	2005 \$
Due from Tay Utility Contracting Inc.	36,593	30,410
Due from Tay Hydro Inc.	48,285	30,602
	84,878	61,012

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2006

3. RELATED PARTY TRANSACTIONS, continued

(d) Balances due to the Township of Tay included in long term debt consists of:

	2006 \$	2005 \$
Due from (to) Township of Tay	-	1,750
Note payable to Township of Tay	1,742,821	1,742,821
Debenture payable to Township of Tay	633,000	830,000
	<u>2,375,821</u>	<u>2,574,571</u>

The note payable, debenture and interest thereon have been recorded in these financial statements at the carrying amounts, which were equal to historical cost or fair value. The interest rate represents fair value as was determined at the time the debt was issued.

4. PROPERTY, PLANT AND EQUIPMENT

	Cost \$	Accumulated amortization \$	2006 Net book value \$	2005 Net book value \$
Buildings	276,277	71,332	204,945	210,152
Distribution system	6,030,128	3,711,623	2,318,505	2,246,821
Land rights	299,804	103,087	196,717	201,443
Other capital assets	637,560	543,076	94,484	74,237
	<u>7,243,769</u>	<u>4,429,118</u>	<u>2,814,651</u>	<u>2,732,653</u>

5. OTHER ASSETS

	2006 \$	2005 \$
Organization costs	16,567	22,089
Optimization study	-	25,480
Restricted cash	-	118,678
	<u>16,567</u>	<u>166,247</u>

Organization costs consist of \$ 27,611 original cost, less accumulated amortization of \$ 11,044. During the year the company charged \$ 5,522 of amortization to operations.

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2006

6. REGULATORY ASSETS

As described in note 2, the company has recorded the following regulatory assets and liabilities.

	\$
Retail settlement variances	(230,871)
Qualifying market transition costs	4,809
Other regulatory assets	48,337
Approved regulatory assets	716,661
Regulatory assets recovered	(441,147)
Regulatory assets	97,789
	\$
Regulatory liability	59,397
Current portion included in accounts payable	(29,376)
Regulatory liability	30,021

7. LONG-TERM DEBT

	2006 \$	2005 \$
Debenture payable	633,000	830,000
Note payable	1,742,821	1,742,821
Promissory notes payable	19,820	19,820
	2,395,641	2,592,641
Less: current portion	(1,952,821)	(1,959,641)
	442,820	633,000

The debenture is payable to the Township of Tay, the shareholder of the company and bears interest at rates of 5.05% to 6%. Principal payments are due annually May 31 until 2009.

The note payable is to the Township of Tay, the shareholder of the parent company. Payments are interest only at 7.25%. The note is due on demand.

The promissory notes are non-interest bearing with no specific terms of repayment.

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2006

7. LONG-TERM DEBT, continued

Scheduled principal re-payments are as follows:

	\$
2007	210,000
2008	223,000
2009	200,000

8. SHARE CAPITAL

Authorized

Unlimited number of common shares

Unlimited number of preference shares

Issued

	2006 \$	2005 \$
1,000 common shares	1,742,821	1,742,821

9. EQUITY ADJUSTMENT

The company has established that the development charges included in the financial statements in prior years should have been recorded as equity and accordingly has made an adjustment to the prior year opening equity to reflect this reclassification.

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2006

10. STATEMENT OF CASH FLOWS

Change in non-cash working capital items

	2006 \$	2005 \$
Increase in accounts receivable	(84,721)	(128,738)
Increase in inventory	(14,185)	(5,036)
Due from related parties	(23,866)	1,088
Increase in prepaid expenses	(20,471)	(9,450)
Decrease (increase) in customer and retailer deposits	22,765	(2,032)
Decrease (increase) in unbilled revenue	(42,092)	76,022
Increase in income taxes payable	141,010	-
Decrease (increase) in income taxes receivable	139,696	(111,510)
Increase (decrease) in accounts payable and accrued liabilities	(236,000)	467,006
	(117,864)	287,350

Other information

Interest paid	190,078	182,958
Interest received	61,691	33,729
Income taxes paid (recovered)	(29,141)	30,810

11. SUBSEQUENT EVENTS

Effective April 30, 2007, Tay Hydro Electric Distribution Company Inc. and Newmarket Hydro Ltd. were amalgamated to form Newmarket-Tay Power Distribution Ltd.

12. PENSION PLAN

The company makes contributions to the Ontario Municipal Employees Retirement Fund (OMERS), which is a multi-employer plan, on behalf of staff. The plan is a defined benefit plan, which specifies the amount of the retirement benefit to be received by the employees based on the length of service and rates of pay. OMERS contributions totaled \$ 53,380 - (2005 - \$ 25,827).

TAY HYDRO ELECTRIC DISTRIBUTION COMPANY INC.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2006

13. CONTINGENT LIABILITY

A class action claiming \$500 million in restitutionary payments plus interest was served on Toronto Hydro on November 18, 1999. The action was initiated against Toronto Hydro Electric Commission as the representative of the Defendant Class consisting of all municipal electric Ontario, which have charged late payment charged on overdue utility bills at any time after April 1, 1981.

The claim is that late payment penalties result in the municipal electric utilities receiving interest at effective rate in excess of 60% per year, which is illegal under Section 347(1)(b) of the Criminal Code.

The Electricity Distributors Association is undertaking the defence of this class action. At this time it is not possible to quantify the effect, if any, on these financial statements, and as such no accrual of any potential liability has been recognized.