Orillia Power Generation Corporation
Financial Statements
December 31, 2007

ORILLIAPOWER

Energizing Our Community

Contents

Grant Thornton

Auditors' report

Grant Thornton LLP
Suite 300
6 West Street N
Orillia, ON
L3V 5B8

T (705) 326-7605
F (705) 326-0837
www.GrantThornton.ca

To the Directors of

Orillia Power Corporation

We have audited the balance sheet of Orillia Power Generation Corporation as at December 31, 2007 and the statements of earnings and retained earnings 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, 2007 and the results of its operations and cash flows for year then ended in accordance with Canadian generally accepted accounting principles.

Grant Thornton LLP

Orillia, Canada

March 18, 2008

Chartered accountants,

Licensed public accountants

Orillia Power Generation Corporation
Statements of Earnings and Retained Earnings

(In Thousands)

Year Ended December 31	2007	2006
Revenue		
Generation	$ [redacted]	
Other		
Costs		
Operations, maintenance and administration		
Amortization		
Earnings from operations		
Interest income		
Interest on long term debt		
Earnings before payments in lieu of taxes		
Payments in lieu of taxes (Note 9)		
Net earnings	$	
Retained earnings, beginning of year	$ [redacted]	
Net earnings		
Dividends		
Retained earnings, end of year	$	

See accompanying notes to the financial statements.

Orillia Power Generation Corporation
Balance Sheet

(In Thousands)

December 31		2007	2006
Assets			
Current			
Cash	$	[redacted]	
Receivables			
Payments in lieu of taxes recoverable			
Prepaids			
Property and equipment (Note 3)			
	$		

Liabilities			
Current			
Payables and accruals	$	[redacted]	
Due to related parties (Note 4)			
Employee future benefits (Note 5)			
Long term debt (Note 6)			
Shareholder's Equity			
Capital stock (Note 7)			
Retained earnings			
	$		

Commitments (Note 8)

On Behalf of the Board

____________ Director ____________ Director

See accompanying notes to the financial statements.

Orillia Power Generation Corporation
Statement of Cash Flows

(In Thousands)

Year Ended December 31		**2007**	2006
Increase (decrease) in cash and cash equivalents			
Operating			
Net earnings	$	[redacted]	[redacted]
Amortization		[redacted]	[redacted]
		[redacted]	[redacted]
Change in non-cash operating working capital (Note 10)		[redacted]	[redacted]
		[redacted]	[redacted]
Financing			
Dividends		[redacted]	[redacted]
Investing			
Net additions to property and equipment		[redacted]	[redacted]
Net increase (decrease) in cash and cash equivalents		[redacted]	[redacted]
Cash and cash equivalents, beginning of year		[redacted]	[redacted]
Cash and cash equivalents, end of year	$	[redacted]	[redacted]

See accompanying notes to the financial statements.

1. Nature of operations

The Company generates electricity under license from the Ontario Energy Board (OEB). The Electricity Act, 1998 provides for a competitive marketplace in the sale of electricity where price is established by the economics of supply and demand. The Company does not bid production into the market but accepts the rate established by the market at time it supplies power into the Provincial grid.

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2. Summary of significant accounting policies

Cash and cash equivalents

Cash and cash equivalents include cash on hand and balances with banks.

Property and equipment

Property and equipment are recorded at cost and include contracted services, materials, labour, engineering costs and overheads. Significant renewals and enhancements to existing assets are capitalized only if the service life of the asset is extended, reliability or productivity is improved above original design standards or associated operating costs are lowered. Maintenance and repair costs are expensed as incurred.

Property and equipment is amortized using the straight-line method over periods approximating its estimated useful life as follows:

Land rights	5	years
Generation stations and buildings	30-50	years
Other capital assets	5-10	years

In the case of capital expenditures that become part of a generating station, that expenditure is amortized over the remaining useful life of the station as a whole. When property and equipment is sold or scrapped, the cost of the asset and the related accumulated amortization is removed when identifiable from the accounts, with the resulting net gain or loss being included in operations for the year.

Corporate income and capital taxes

Under the Electricity Act, 1998, the Company is required to make payments in lieu of corporate taxes to Ontario Electricity Financial Corporation (OEFC). These payments are calculated in accordance with the rules for computing income and taxable capital and other relevant amounts contained in the Income Tax Act (Canada) and the Corporations Tax Act (Ontario) as modified by the Electricity Act, 1998 and related regulations.

2. Summary of significant accounting policies (Continued)

Corporate income and capital taxes (Continued)

The Company provides for payments in lieu of corporate income taxes relating to its regulated business using the taxes payable method as directed by the OEB. 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 for accounting purposes. This regulation accounting treatment differs from Canadian generally accepted accounting principles for enterprises operating in a non-regulated environment.

Employee future benefits

Pension plan
The Company provides pension benefits for its employees through the Ontario Municipal Employees Retirement System (OMERS). This multi-employer pension plan provides pensions for employees of Ontario municipalities, local boards, public utilities and school boards. It is a contributory defined benefit pension plan financed by equal contributions from participating employers and employees and by investment earnings of the fund. The Company recognizes the expense related to this plan as contributions are made.

Employee future benefits other than pension plan
The Company provides life insurance benefits to employees hired prior to January 1, 2008 when they are no longer providing active service. Employee future benefits expense is recognized in the period in which the employee renders services. Employee future benefits other than pension plans are recorded on an accrual basis. The accrued benefit obligation and current service costs are calculated using the projected benefit method pro-rated on service and based on assumptions that reflect management's best estimate. The current service cost for a period is equal to the present value of expected future benefits attributed to employee's services rendered in the period.

Fixed assets 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. An equivalent amount is capitalized as an inherent cost of the associated fixed assets.

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 date can be determined and, consequently, a reasonable estimate of the fair value of any asset retirement obligations can not be made at this time.

Orillia Power Generation Corporation
Notes to the Financial Statements

(In Thousands)
December 31, 2007

2. Summary of significant accounting policies (Continued)

Revenue recognition

Revenue is recognized in the period power is generated at rates established by the electricity market.

Use of estimates

The preparation of financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenditures for the year. Actual results could differ from these estimates.

3. Property and equipment

		2007		2006
	Cost	Accumulated Amortization	Net Book Value	Net Book Value
Land	$ [redacted]			
Land rights				
Buildings				
Generating stations				
Other capital assets				
	$			

4. Related party transactions

Transactions involving the sale of electricity are in the normal course of operations and are measured at the exchange amount, which is equal to the fair value as prescribed by regulation. Transactions involving other services have been recorded in these financial statements at the carrying amounts, which were equal to historical cost or fair value. Fair values represent fees for equivalent services provided to third parties in the normal course of operations as prescribed by regulations. The Company had the following related party transactions:

	2007	2006
Orillia Power Distribution Corporation – related Company		
Services purchased	$ [redacted]	
Services provided		
Power generated and supplied on behalf of Orillia customers		

Orillia Power Generation Corporation
Notes to the Financial Statements

(In Thousands)
December 31, 2007

4. Related party transactions (Continued)

		2007	2006
City of Orillia - the shareholder of Orillia Power Corporation, the parent Company			
Services purchased	$	[redacted]	
Services provided			
Interest expense			
Balance outstanding at December 31:			
Due to Orillia Power Distribution Corporation – related Company	$		

During the year, the Company paid interest of [redacted] on a promissory note payable, to the City of Orillia, the shareholder of Orillia Power Corporation, the parent Company. Included in payables and accruals is $[redacted] due to the City of Orillia.

5. Employee future benefits

Pension plan
Current service contributions to OMERS for 2007 were [redacted]

Employee future benefits other than pension plan
The Company measures its accrued benefits obligation for accounting purposes as at December 31 of each year. The latest actuarial valuation was performed as at December 31, 2006. Key economic assumptions used to determine the valuation are Consumer Price Index; 2% per annum, discount rate; 5% per annum and salary increase rate; 3.3%. A reconciliation of the Company's accrued benefits obligation is as follows:

		2007	2006
Employee future benefits obligation, beginning of year	$	[redacted]	
Current service cost			
Interest on benefits obligation			
Benefit plan payments			
Employee future benefits obligation, end of year	$		

6. Long term debt

The promissory note payable to the City of Orillia, the shareholder of Orillia Power Corporation, the parent Company, bears interest for the current year at [redacted] per annum [redacted] The interest rate is reviewed annually. Payments of interest are required to be made quarterly on the last day of March, June, September and December. The promissory note is due December 31, 2030.

7. Capital stock

	2007	2006

Authorized:
The Company is authorized to issue an unlimited number of common shares.

Issued:

1,001 shares	$ [redacted]	

8. Commitments

Parks Canada license renewal
In 2004, the Company agreed in principle to a license renewal with Parks Canada – Trent Severn Waterway, which includes the right to use surplus water at the Swift Rapids Generating Station. In 2005, it was determined by the Federal Department of Justice that the Company would be required to make application for a new license to operate the plant in order to ensure compliance under the Dominion Waterpower Act. During 2006, the Company made application for and was granted the right to continue operating the plant under license. The Company is currently in discussions with Parks Canada to finalize the wording and execute the license.

Donation
During 2007, the Company pledged to make a donation of [redacted] for five years to assist with the funding requirements of the local hospital expansion. Total payments of [redacted] have been made to satisfy this pledge to date.

9. Payments in lieu of taxes

The provision for payments in lieu of corporate income taxes (PILS) differs from the amount that would have been recorded using the combined Canadian Federal and Ontario statutory income tax rate. The reconciliation between the statutory rate and effective tax rates is provided as follows:

		2007	2006
Earnings before provision for PILS	$	[redacted]	
Federal and Ontario statutory income tax rates			
Provision for PILS at statutory rate	$		
Increase (decrease) resulting from:			
Temporary differences			
Capital cost allowance in excess of amortization			
Adjustment to prior year provision			
Net temporary differences			
Permanent differences			
Capital cost allowance on appraisal increment			
Manufacturing and processing deduction			
Dividend refund			
Other			
Net permanent differences			
Provision for PILS	$		
Effective income tax rate			

Future income taxes have not been recorded as they are expected to be reflected through future rates. Significant components of the Company's deductible timing differences at year end are related to property and equipment [redacted].

10. Supplemental cash flow information

	2007	2006
Change in non-cash operating working capital		
Receivables	$ [redacted]	
Payments in lieu of taxes recoverable		
Prepaids		
Payables and accruals		
Due to related parties		
Payments in lieu of taxes		
	$	
Interest received	$	
Interest paid	$	
Payment in lieu of taxes paid (net)	$	

11. Public liability insurance

The Company is a member of the Municipal Electric Association Reciprocal Insurance Exchange (MEARIE), which was created on January 1, 1987. A reciprocal insurance exchange may be defined as a group of persons formed for the purpose of exchanging reciprocal contracts of indemnity or inter-insurance with each other through the same attorney. MEARIE has provided general liability insurance to the Company of [redacted] per occurrence.

12. Financial instruments

Financial instruments consist of cash, receivables, payables and accruals, due to related parties, payments in lieu of taxes recoverable 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 value of these financial instruments approximates their carrying values, unless otherwise noted.

13. Comparative figures

Certain of the comparative figures have been reclassified to conform to the financial statement presentation adopted for the current year.

14. Future accounting pronouncements

Accounting pronouncements that will come into effect during 2008 and 2009 are listed below. The Company is currently assessing the potential impact that each of the following new standards will have on its financial statements.

Financial instruments, hedges, and comprehensive income

Effective January 1, 2008, the Company will be required to adopt CICA Handbook Section 3855, "Financial Instruments - Recognition and Measurement"; Section 3865 "Hedges"; and Section 1530 "Comprehensive Income". Under the new standards, all financial assets must be classified as held-to-maturity, loans and receivables, held-for-trading or available-for-sale and all financial liabilities must be classified as held-for-trading and other. Financial instruments classified as held-for-trading will be measured at fair value with changes in fair value recognized in net income. Financial assets classified as held-to-maturity or as loans and receivables and financial liabilities not classified as held-for-trading will be measured at amortized cost. Available-for-sale financial assets will be measured at fair value with changes in fair value recognized in other comprehensive income. All derivative financial instruments will be reported on the balance sheet at fair value with changes in fair value recognized in net income unless the derivative is part of a hedging relationship. The new standards will also require presentation of a separate statement of comprehensive income.

Financial instruments disclosures and presentation

Effective January 1, 2008, the Company will be required to adopt CICA Handbook Section 3862 "Financial Instruments – Disclosures" and Section 3863 "Financial Instruments – Presentation" which will replace Section 3861, Financial Instruments – Disclosure and Presentation. The new disclosure standard increases the emphasis on the risks associated with both recognized and unrecognized financial instruments and how these risks are managed. The presentation standard carries forward former presentation requirements that are unchanged.

Capital disclosures

Effective January 1, 2008, the Company will be required to adopt CICA Handbook Section 1535 "Capital Disclosures". The new standard requires disclosure of an entity's objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital and whether the entity has complied with any capital requirements and, if it has not complied, the consequences of such non-compliance.

Inventories

Effective January 1, 2008, the Company will be required to adopt CICA Handbook Section 3031 "Inventories". This new standard replaces the existing Section 3030 of the same name and contains requirements on measurement and disclosure of inventories and revises and enhances the requirements for assigning costs to inventories. This new standard also allows for reversal of previous write-downs.

14. Future accounting pronouncements (Continued)

General standards on financial statement presentation

Effective January 1, 2008, the Company will be required to adopt CICA Handbook Section 1400 "General Standards on Financial Statement Presentation". This new standard amends the previous standard to include requirements to assess and disclose an entity's ability to continue as a going concern.

Rate regulated operations

Effective January 1, 2009, the Company will be required to adopt changes to the CICA Handbook regarding rate regulated operations. The temporary exemption of Section 1100 that provided relief from the requirement to apply the Section to the recognition and measurement of assets and liabilities arising from rate regulation will be removed. Section 3465 will be amended to require the recognition of future income tax liabilities and assets as well as a separate regulatory asset or liability for the amount of future income taxes expected to be included in future rates and recovered from or paid to future customers.

There will be adjustments within AcG-19 to reflect the changes made for Sections 1100 and 3465 of the CICA Handbook.