

**FINANCIAL STATEMENTS OF
NEWMARKET HYDRO LTD.**

December 31, 2005

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AUDITORS' REPORT

To the Shareholder of
Newmarket Hydro Ltd.

We have audited the balance sheet of Newmarket Hydro Ltd. as at December 31, 2005 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, 2005 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, 2004 and for the year then ended were audited by another firm of Chartered Accountants who expressed an opinion without reservation on those statements in their report dated May 13, 2005.

Collins Barrow Kawarthas

Chartered Accountants

Peterborough, Ontario
April 7, 2006

NEWMARKET HYDRO LTD.

BALANCE SHEET

As at December 31, 2005

	2005 \$	2004 \$
ASSETS		
Current assets		
Cash	13,635,617	8,491,281
Short term investments (note 3)	412,700	2,888,450
Accounts receivable	3,722,524	4,531,234
Unbilled revenue	6,312,983	6,016,260
Income taxes receivable (note 4)	224,077	-
Inventory	773,894	862,954
Prepaid and other	217,558	170,675
	25,299,353	22,960,854
Regulatory Assets (note 5)	1,843,581	984,576
Property, plant and equipment (note 6)	38,692,094	38,398,426
	65,835,028	62,343,856
LIABILITIES AND SHAREHOLDER'S EQUITY		
Current liabilities		
Accounts payable and accrued liabilities (note 7)	8,712,123	6,892,784
Income taxes payable	-	299,448
Deferred revenue	1,619,831	774,362
Due to Newmarket Hydro Holdings Inc. (note 8)	1,138,958	1,334,176
Current portion of deposits held	352,586	952,586
	11,823,498	10,253,356
Deposits held	2,283,888	2,190,679
Employee future benefits (note 9)	613,643	514,043
Note payable (note 10)	22,000,000	22,000,000
	36,721,029	34,958,078
Shareholder's equity		
Share capital (note 11)	25,806,563	25,806,563
Retained earnings	3,307,436	1,579,215
	29,113,999	27,385,778
	65,835,028	62,343,856

On behalf of the Board

Director

Director

The accompanying notes are an integral part of these financial statements

NEWMARKET HYDRO LTD.
STATEMENT OF RETAINED EARNINGS

For the year ended December 31, 2005

	2005 \$	2004 \$
Retained earnings - beginning of year	1,579,215	777,151
Net income for the year	1,928,221	802,064
Dividend paid on common shares	(200,000)	-
Retained earnings - end of year	3,307,436	1,579,215

The accompanying notes are an integral part of these financial statements

NEWMARKET HYDRO LTD.
STATEMENT OF INCOME

For the year ended December 31, 2005

	2005 \$	2004 \$
Service Revenue	66,616,693	57,539,288
Cost of power	53,647,628	45,564,723
Gross profit	12,969,065	11,974,565
Expenses		
Amortization	3,001,408	2,859,680
Donations (note 8)	1,885,000	1,500,000
System operation and maintenance	1,718,331	1,965,592
Interest	1,709,512	1,624,882
Administration	1,691,114	1,996,309
Customer billing and collecting	1,266,615	1,449,131
Property and capital taxes	225,678	231,561
	11,497,658	11,627,155
Income before undernoted items and income taxes	1,471,407	347,410
Other income		
Service and retailer charges	120,627	119,273
Interest	304,596	234,887
Occupancy, connection and collection fees	515,489	485,173
Rentals and miscellaneous	167,008	105,427
Gain on disposal of capital assets	25,700	70,936
	1,133,420	1,015,696
Income before income taxes	2,604,827	1,363,106
Provision for income taxes	676,606	561,042
Net income for the year	1,928,221	802,064

The accompanying notes are an integral part of these financial statements

NEWMARKET HYDRO LTD.

STATEMENT OF CASH FLOWS

For the year ended December 31, 2005

	2005 \$	2004 \$
Operating activities		
Net income for the year	1,928,221	802,064
Adjustments for		
Amortization	3,362,421	3,249,585
Employee future benefits	99,600	142,473
Gain on disposal of capital assets	(25,700)	(70,936)
	5,364,542	4,123,186
Changes in non-cash working capital items		
Decrease in short term investments	2,475,750	114,275
Decrease (increase) in accounts receivable	808,710	(139,831)
Increase in unbilled revenue	(296,723)	(915,166)
Increase in income taxes receivable	(523,525)	-
Decrease (increase) in inventory	89,060	(139,283)
Decrease (increase) in prepaid and other	(46,883)	107,589
Increase in accounts payable and accrued liabilities	1,819,339	1,621,241
Increase (decrease) in deferred revenue	845,469	(17,549)
Decrease in due from IESO	-	644,799
	10,535,739	5,399,261
Investing activities		
Proceeds on disposal of property, plant and equipment	39,959	70,936
Purchase of property, plant and equipment	(3,670,348)	(5,020,832)
Increase in regulatory assets	(859,005)	(251,090)
	(4,489,394)	(5,200,986)
Financing activities		
Deposits held	(506,791)	323,223
Due to Newmarket Hydro Holdings Inc.	(195,218)	(3,060,849)
Dividend paid on common shares	(200,000)	-
	(902,009)	(2,737,626)
Increase (decrease) in cash	5,144,336	(2,539,351)
Cash - beginning of year	8,491,281	11,030,632
Cash - end of year	13,635,617	8,491,281
Other information		
Interest paid	1,709,512	1,341,159
Interest received	304,596	234,887
Income taxes paid	1,057,000	779,800
Dividends paid	200,000	-

The accompanying notes are an integral part of these financial statements

NEWMARKET HYDRO LTD.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2005

1. NATURE OF OPERATIONS

Newmarket Hydro Ltd. (the Company) is a wholly-owned subsidiary of Newmarket Hydro Holdings Inc. and was incorporated April 10, 2000 under the Business Corporations Act of the Province of Ontario. The Company commenced operations on November 1, 2003. Newmarket Hydro Holdings Inc. is wholly-owned by the Town of Newmarket.

The principal activity of the Company is to distribute electricity to the residents and businesses in the Town of Newmarket under license issued by the Ontario Energy Board (OEB). The Company is regulated by the OEB and adjustments to its distribution and power 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, 2005 are disclosed in Note 5. The Company continually assesses the likelihood of the recovery of these assets. If recovery is no longer considered probable, the amounts 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. Additional details related to the calculation and method of accounting for PILS is included at Note 4.

NEWMARKET HYDRO LTD.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2005

2. SIGNIFICANT ACCOUNTING POLICIES, continued

(b) *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.

(c) *Short term investments*

Short term investments are carried at the lower of cost and market value.

(d) *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 parts and materials used for maintenance and capital projects.

(e) *Property, plant and equipment*

Property, plant and equipment are stated at cost which is comprised of material, labour, charges for truck time and overheads. Amortization is provided on a straight-line basis over the estimated service lives of the assets as follows:

Transmission and distribution systems	25 to 30 years
Office equipment	3 to 10 years
Plant and equipment	10 to 15 years
Leasehold improvements	10 years

Contributions for capital construction consist of third party contributions toward the cost of constructing distribution assets. The third party contribution is calculated through an economic evaluation as per the OEB Distribution Service Code. Contributed capital amounts are recorded as received and amortized over the same period as the asset to which they relate being 25 to 30 years.

(f) *Financial instruments*

The Company's financial instruments consist of cash, term deposits and short-term investments, accounts receivable and unbilled revenue, accounts payable and accrued liabilities, advances from related parties and notes payable. Unless otherwise noted it is management's opinion that the Company is not exposed to significant interest, currency or credit risks.

NEWMARKET HYDRO LTD.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2005

2. SIGNIFICANT ACCOUNTING POLICIES, continued

(g) *Deferred revenue*

Deferred revenue represents amounts received from customers in advance of energy usage and amounts received from the OEB related to Conservation Demand Management funds received and not expended in the current year.

(h) *Related party transactions*

Related party transactions are in the normal course of operations and have been measured at the exchange amount which is the amount of consideration established and agreed to by the related parties. Related party transactions and balances are detailed in Note 8.

(i) *Post-employment benefits*

The Company pays certain health, dental and life insurance benefits on behalf of its retired employees. The Company recognizes these post-retirement costs in the period in which the employees rendered the services.

The transitional obligation resulting from the implementation of this policy in 2000 (applied on a prospective basis) is being amortized over the average remaining service period of employees being 14 years.

(j) *Revenue recognition*

Service revenue is 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 the Independent Electricity System Operator.

(k) *Reclassification*

Certain reclassifications have been made to the 2004 financial statements to conform with the presentation used in 2005.

NEWMARKET HYDRO LTD.
NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2005

5. REGULATORY ASSETS

The Company has accumulated certain variance accounts representing purchase of power costs in excess of revenue billed to customers. The OEB regulates both the amounts that can be charged to the Company and the rates that the Company bills to its customers. In 2002, an amount of \$ 2,713,020 representing specific variance accounts was written off since management assessed the likelihood of future recovery to be low. In 2003, the Ontario government introduced Bill 4 which permitted Local Distribution Companies (LDC's) to recover regulatory assets and variance accounts over a four year period starting April 1, 2004. The amounts written off in 2002 are being recorded as received. The amount received and recorded in 2005 related to these accounts totalled \$ 924,419 (2004 - \$ 574,663).

The Company has recorded the following Regulatory Assets:

	2005 \$	2004 \$
Trust bank account balance	-	2
Deferred qualifying transition costs	203,671	337,820
Retail settlement variances	1,639,910	646,754
	1,843,581	984,576

6. PROPERTY, PLANT AND EQUIPMENT

	2005		2004	
	Cost \$	Accumulated Amortization \$	Net book value \$	Net book value \$
Land	1,458,530	-	1,458,530	1,208,723
Transmission and distribution systems	69,647,966	34,353,162	35,294,804	35,018,394
Office equipment	1,297,457	815,652	481,805	341,262
Plant and equipment	4,019,711	2,676,892	1,342,819	1,666,482
Leasehold improvements	347,913	233,777	114,136	163,565
	76,771,577	38,079,483	38,692,094	38,398,426

NEWMARKET HYDRO LTD.
NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2005

7. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	2005 \$	2004 \$
Accounts payable - purchased power	5,296,902	4,197,104
Fixed energy rate rebate payable	1,008,761	26,560
Other accounts payable and accrued liabilities	1,366,084	1,807,213
Water and sewer billings payable	1,040,376	861,904
	8,712,123	6,892,781

8. DUE TO RELATED PARTIES AND RELATED PARTY TRANSACTIONS

- (a) During the year the Company entered into transactions with its parent, Newmarket Hydro Holdings Inc. (NHHI) and with The Town of Newmarket which is the sole shareholder of Newmarket Hydro Holdings Inc. Revenue charged during the year included energy, street light capital and street light maintenance charged at commercial rates to the Town of Newmarket.

In addition, included in amounts payable are water and sewer amounts collected which are due to the Town. These amounts are collected and remitted in accordance with a contract with URB Olameter and remitted on their behalf.

NEWMARKET HYDRO LTD.
NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2005

8. DUE TO RELATED PARTIES, continued

(b) Details of transactions with the Town of Newmarket during the year are as follows:

	2005 \$	2004 \$
Revenue		
Energy sales	1,622,892	1,643,665
Services - Street light capital	57,082	134,395
Services - Street light maintenance	224,396	224,396
	-	-
	1,904,370	2,002,456
Expenses		
Interest	1,662,000	1,595,000
Donations	1,885,000	1,500,000
Rent, property tax and other	339,054	307,915
Other		
Purchase of land	115,000	1,064,200

(c) The following amounts due to/from the Town of Newmarket are included in the financial statements:

	2005 \$	2004 \$
Accounts receivable	154,689	278,514
Accounts payable	44,000	591,306

NEWMARKET HYDRO LTD.
NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2005

3. SHORT TERM INVESTMENTS

Short term investments consist of:

	2005 \$	2004 \$
Province of Saskatchewan Bond	-	2,888,450
Corporate bonds	412,700	-
	412,700	2,888,450

The market value of the investments at December 31, 2005 is \$ 416,152 (2004 - \$ 2,888,450).

4. INCOME TAXES RECEIVABLE

As described in Note 2, the Company is required to make payments-in-lieu of income taxes. Future income taxes are not recorded in the accounts since the Company follows the taxes payable method. The future tax asset balance is \$ 3,806,194 (2004 - \$ 3,664,478). This asset is determined by calculating the difference between the tax basis of the asset and its carrying amount on the balance sheet. Future tax assets are calculated using tax rates anticipated to apply in the periods that the temporary differences are expected to be recovered or settled.

NEWMARKET HYDRO LTD.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2005

9. EMPLOYEE FUTURE BENEFITS

The Company provides certain health, dental and life insurance benefits for retired employees pursuant to the Company's policy. The accrued benefit obligation and net periodic expense for the year were determined by actuarial valuation. The most recent valuation was performed December 31, 2004. Information about the Company's defined benefit plan is included in the table which follows.

Significant actuarial assumptions employed for the valuations are as follows: future general inflation level of 2.1%, discount rate of 5.75%, salary and wage level increases at 3% per annum. For measurement purposes, a 9% annual increase in the per capita cost of health benefits was assumed for 2005. The rate was assumed to decrease annually by 1% to a rate of 5% for 2009 and thereafter. A 5% annual rate of increase in the per capita cost of covered dental costs was assumed for 2005 and thereafter.

	2005 \$	2004 \$
Accrued Benefit Obligation, beginning of year	514,043	371,570
Current service cost	76,873	68,572
Amortization of the transitional obligation	37,727	37,727
Actuarial loss for the year	-	51,227
Benefits paid	(15,000)	(15,053)
Accrued Benefit Obligation, end of year	613,643	514,043
Unamortized Transitional Obligation	188,635	226,362
Accrued Benefits Liability	802,278	740,405

10. NOTE PAYABLE

	2005 \$	2004 \$
Note payable	22,000,000	22,000,000

The note payable is an unsecured promissory note to the Town of Newmarket. The note bears interest at a rate of 7.25% per annum, paid quarterly in arrears. Changes to the terms of the note require 13 months notice. The note has been subordinated to the IESO letter of credit referred to in Note 12.

NEWMARKET HYDRO LTD.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2005

11. SHARE CAPITAL

	2005 \$	2004 \$
Authorized Unlimited number of common shares		
Issued 1,001 common shares	25,806,563	25,806,563

12. SHORT TERM CREDIT FACILITIES

The Company has a \$ 1,500,000 operating loan available from a major chartered bank. The facility is a 364 day revolving operating loan, bearing interest at prime, to be repaid with one year from date of acquisition unless extended by the bank. A standby fee of 10 basis points, payable quarterly in arrears applies to any unused portion of the facility. As at the balance sheet date, the Company has no balance outstanding on this facility. The operating loan includes restrictive clauses with respect to repayment.

The Company has provided prudential support in the amount of \$ 5,406,833 to the Independent Market Operator. The prudential support is secured by a letter of credit with a major chartered bank for \$ 8,505,000 and contains restrictive clauses with respect to debt repayments.

13. COMMITMENTS

The Company has a five-year lease agreement, which expires in 2006 with the Town of Newmarket for the rental of the 590 Steven Court building. The annual rent payments are \$ 180,500, paid quarterly on the last day of the fiscal quarter.

Pursuant to the Ontario Energy Board's EB-2005-0315, Newmarket Hydro Ltd. has been instructed to participate in the construction of the Holland Junction transformer station in order to provide additional electricity supply to the northern York Region. The total cost of the Holland Junction transformer station is estimated to be 13.85 million dollars and the estimated completion date is summer 2008. The Company's share of the cost is estimated to be 4 million dollars. Costs of \$ nil related to the project were incurred in 2005.

The Government of the Province of Ontario through Bill 21 has indicated that 800,000 "Smart Meters" will be installed throughout the province by 2007 and that every meter will be a smart meter by 2010. The exact cost to implement the project in the Town of Newmarket is unknown, however, the Company anticipates that the cost could result in a capital outlay of over 3 million dollars.

NEWMARKET HYDRO LTD.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended December 31, 2005

14. PENSION AGREEMENT

The Company makes contributions to the Ontario Municipal Employees' Retirement Fund (OMERs), which is a multi-employer plan, on behalf of its employees. The plan is a defined benefit plan which specifies the amount of retirement benefits to be received by the employees based on the length of service and rates of pay.

The amount contributed to OMERS for 2005 was \$ 196,080 (2004 - \$ 183,146) for current service.

15. CONTINGENCIES

(a) In the normal course of business, the Company enters into agreements that meet the definition of a guarantee. The guarantees include indemnities under lease agreements, purchase and sale agreements, confidentiality agreements, outsourcing, service and information agreements. The nature of these indemnification agreements prevents the Company from making a reasonable estimate of the maximum exposure due to the difficulties in assessing the amount of liability related to the likelihood and predictability of future events. Historically, the Company has not made any significant payments under similar indemnification agreements and therefore no amount has been accrued in the financial statements with respect to these agreements.

(b) Indemnity has been provided to all directors and/or officers of the Company for various items including, but not limited to, all costs to settle suits or actions due to association with the Company, subject to certain restrictions. The Company has purchased directors' and officers' liability insurance to mitigate the cost of any potential suits or actions. The amount of any potential future liability which exceeds the amount of insurance coverage cannot be reasonably be determined.

(c) The Company participates with other municipal utilities in Ontario in an agreement to exchange reciprocal contracts of indemnity through the Municipal Electric Association Reciprocal Insurance Exchange. Under this agreement, the Company is contingently liable for additional assessments to the extent that premiums collected are not sufficient to cover actual losses, claims and costs experienced.

(d) A class action claiming \$ 500 million in restitutionary payments plus interest was served on Toronto Hydro on November 18, 1998. The action was initiated against Toronto Hydro Electric Commission as a representative of the Defendant Class consisting of all municipal electric utilities in Ontario which have charged late payment charges on overdue utility bills at any time after April 1, 1981.

The claim is that late payment penalties result in municipal electrical utilities receiving interest at effective rates 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.