

Barrie Hydro Distribution Inc.
Financial Statements
For the year ended December 31, 2006

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For the year ended December 31, 2006

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Auditors' Report

**To the Shareholder of
Barrie Hydro Distribution Inc.**

We have audited the balance sheet of Barrie Hydro Distribution Inc. as at December 31, 2006 and the statements of operations and retained earnings and cash flows for the year then ended. These financial statements are the responsibility of the corporation'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 corporation as at December 31, 2006 and the results of its operations and cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

BDO Dunwoody LLP

Chartered Accountants

Barrie, Ontario
March 16, 2007

**Barrie Hydro Distribution Inc.
Balance Sheet**

December 31	2006	2005
Assets		
Current		
Cash (Note 1)	\$ 2,186,053	\$ 9,225,335
Accounts receivable	11,714,935	8,699,780
Unbilled service revenue	13,506,096	14,899,271
Inventories	1,575,759	1,240,842
Prepaid expenses	702,882	376,753
	29,685,725	34,441,981
Property, plant and equipment (Note 2)	122,302,120	115,164,862
Construction in progress (Note 2)	2,420,821	4,033,601
Long-term investment (Note 3)	71,785	71,785
Goodwill	9,554,075	9,554,075
Deferred charges and other long-term assets (Note 4)	1,058,687	929,593
Regulatory assets (Note 5)	-	1,864,343
	\$165,093,213	\$166,060,240

Liabilities and Shareholder's Equity

Current		
Accounts payable and accrued liabilities	\$ 15,532,928	\$ 21,395,972
Construction deposits	1,143,500	1,083,798
Payments in lieu of corporate taxes payable	969,164	911,607
Due to related parties (Note 6)	2,428,521	3,149,027
Customer deposits	1,913,168	1,788,084
Current portion of obligations under capital leases (Note 10)	54,372	51,171
	22,041,653	28,379,659
Customer deposits	2,624,808	2,413,565
Regulatory liabilities (Note 5)	1,657,769	-
Other long-term liabilities (Note 7)	244,114	268,981
Employee future benefits (Note 8)	2,571,708	2,371,626
Long-term debt (Notes 6 and 9)	45,000,000	45,000,000
Obligations under capital leases (Note 10)	64,892	119,265
Subdivision deposit rebates (net of refunds)	13,332,283	11,537,063
	87,537,227	90,090,159
Contingent liabilities (Note 13)		
Shareholder's equity		
Share capital (Note 14)	61,491,374	61,491,374
Retained earnings	16,064,612	14,478,707
	77,555,986	75,970,081
	\$165,093,213	\$166,060,240

On behalf of the Board:



Director



Director

The accompanying summary of significant accounting policies and notes are an integral part of these financial statements.

**Barrie Hydro Distribution Inc.
Statement of Operations and Retained Earnings**

For the year ended December 31	2006	2005
Service revenue		
Residential	\$ 17,877,570	\$ 17,169,125
Commercial (Note 6)	10,504,721	9,984,734
Street lighting	93,331	90,966
	28,475,622	27,244,825
Service revenue adjustments	61,613	535,834
	28,537,235	27,780,659
Cost of power revenue	110,243,230	119,056,463
	138,780,465	146,837,122
Cost of power	110,243,230	119,056,463
Distribution revenue	28,537,235	27,780,659
Other revenue		
Customers' forfeited discounts and late payment charges	521,785	506,118
Water and sewer billing collection services (Note 6)	1,480,731	1,411,216
Other revenue	1,943,287	1,634,061
	3,945,803	3,551,395
	32,483,038	31,332,054
Expenditures		
Administration and general (Note 6)	7,084,216	6,689,413
Amortization	8,432,623	7,245,178
Interest on long-term debt (Note 6)	2,912,508	3,112,500
Other interest	313,769	442,671
Operation maintenance	3,804,017	3,365,508
	22,547,133	20,855,270
	9,935,905	10,476,784
Provision for payments in lieu of corporate income taxes, capital taxes and Part 1.3 tax on large corporations (Note 16)	(5,450,000)	(4,700,578)
Net income for the year	4,485,905	5,776,206
Retained earnings, beginning of year	14,478,707	10,531,501
Dividends (Notes 6 and 15)	(2,900,000)	(1,829,000)
Retained earnings, end of year	\$ 16,064,612	\$ 14,478,707

The accompanying summary of significant accounting policies and notes are an integral part of these financial statements.

**Barrie Hydro Distribution Inc.
Statement of Cash Flows**

For the year ended December 31	2006	2005
Cash flows from operating activities		
Net income for the year	\$ 4,485,905	\$ 5,776,206
Adjustments for		
Amortization of property, plant and equipment	8,432,623	7,245,178
Gain on disposal of property, plant and equipment	(14,839)	(82,872)
Amortization of deferred charges	185,768	307,371
	13,089,457	13,245,883
Changes in non-cash operating working capital		
Accounts receivable	(3,015,155)	2,368,026
Inventories	(334,918)	(111,816)
Prepaid expenses	(326,129)	(30,878)
Unbilled service revenue	1,393,175	(2,306,405)
Accounts payable and accrued liabilities	(5,863,042)	6,045,333
Construction deposits	59,703	(739,886)
Due to related parties	(520,506)	(433,668)
Other long-term liabilities	(24,867)	3,022
Payments in lieu of corporate taxes payable	57,557	(1,215,568)
	(8,574,182)	3,578,160
	4,515,275	16,824,043
Cash flows from investing activities		
Expenditures on property, plant and equipment and construction in progress	(12,161,883)	(7,467,407)
Increase in deferred charges	(314,862)	-
Proceeds on sale of property, plant and equipment	14,839	268,565
Net decrease in regulatory assets	1,864,343	1,305,245
	(10,597,563)	(5,893,597)
Cash flows from financing activities		
Customer deposits	336,327	(1,858,587)
Net increase in regulatory liabilities	1,657,769	-
Increase in employee future benefits	200,082	200,004
Net advances from (repayment of) capital lease obligations	(51,172)	96,697
Dividends	(3,100,000)	(1,279,000)
	(956,994)	(2,840,886)
Increase (decrease) in cash during the year	(7,039,282)	8,089,560
Cash, beginning of year	9,225,335	1,135,775
Cash, end of year	\$ 2,186,053	\$ 9,225,335

The accompanying summary of significant accounting policies and notes are an integral part of these financial statements.

Barrie Hydro Distribution Inc. Summary of Significant Accounting Policies

December 31, 2006

Nature of Business	<p>The corporation was incorporated on October 19, 2000 under the laws of Ontario and is licensed by the Ontario Energy Board ("OEB") as an electricity distributor.</p> <p>The principal activity of the corporation is to distribute electricity to the City of Barrie, and the towns of Bradford West Gwillimbury, Thornton, New Tecumseth and Penetanguishene.</p> <p>The corporation is regulated by the OEB under authority of the Ontario Energy Board Act, 1998.</p>
Basis of Accounting	<p>The financial statements of Barrie Hydro Distribution Inc. are prepared by management in accordance with Canadian generally accepted accounting principles (GAAP) and accounting policies provided by its regulator, the OEB, as contained in the Accounting Procedures Handbook for Electric Distribution Utilities ("AP Handbook"), issued under the authority of the Ontario Energy Board Act, 1998.</p> <p>Due to the regulatory framework the timing of recognition of revenues and expenses and the measurement of certain assets and liabilities may differ from that otherwise expected under Canadian generally accepted accounting principles (GAAP) for non-rate regulated enterprises. Please refer to accounting policies for Spare Transformers and Meters, Post 1999 Contributed Capital, Regulatory Assets and Liabilities, and Payments in lieu of corporate income taxes and capital taxes.</p> <p>The financial statements reflect the significant accounting policies summarized below.</p>
Seasonality of Operations	<p>The corporation's operations are seasonal. Electricity consumption is typically highest in the summer and winter months, July through September and January through March.</p>
Regulation and Rate Setting	<p>The corporation is required to follow regulations as set by the OEB. The OEB approves and sets rates for the transmission and distribution of electricity, ensures distribution companies fulfil their obligations to connect and service customers, and has the authority to provide rate protection for certain electricity customers.</p> <p>The OEB sets rates on an annual basis with rates becoming effective on May 1st through April 30th of the following year. The regulation and monitoring of Ontario's Energy Sector is completed by the OEB through application of codes, rules and guidelines, the licensing of market participants, assisting firms with the management of regulatory requirements, monitoring and enforcing compliance and adjudication.</p>

Barrie Hydro Distribution Inc. Summary of Significant Accounting Policies

December 31, 2006

Inventories	Inventories consist of parts, supplies and materials held for future capital expansion or maintenance and are stated at the lower of average cost and replacement cost.																								
Property, Plant and Equipment	<p>Property, plant and equipment are recorded at cost less accumulated amortization. Costs may include material, labour, contracted services, overhead, engineering costs, and interest on funds used during construction when applicable. Also included in property, plant and equipment is the costs of property, plant and equipment constructed by developers or customers and contributed to the corporation.</p> <p>Upon disposal the cost and accumulated amortization related to the asset are removed and any gains or losses on disposal are credited or charged to other income on the statement of operations.</p> <p>Amortization based on the estimated useful life of the asset is calculated as follows:</p> <table><tr><td>Land rights</td><td>- up to 50 years</td><td>straight-line basis</td></tr><tr><td>Buildings</td><td>- 30 to 60 years</td><td>straight-line basis</td></tr><tr><td>Distribution system</td><td>- 25 to 30 years</td><td>straight-line basis</td></tr><tr><td>General office equipment</td><td>- 10 years</td><td>straight-line basis</td></tr><tr><td>Computer equipment</td><td>- 5 years</td><td>straight-line basis</td></tr><tr><td>Computer software</td><td>- 3 years</td><td>straight-line basis</td></tr><tr><td>Rolling stock</td><td>- 5 to 8 years</td><td>straight-line basis</td></tr><tr><td>Other equipment</td><td>- 10 to 25 years</td><td>straight-line basis</td></tr></table>	Land rights	- up to 50 years	straight-line basis	Buildings	- 30 to 60 years	straight-line basis	Distribution system	- 25 to 30 years	straight-line basis	General office equipment	- 10 years	straight-line basis	Computer equipment	- 5 years	straight-line basis	Computer software	- 3 years	straight-line basis	Rolling stock	- 5 to 8 years	straight-line basis	Other equipment	- 10 to 25 years	straight-line basis
Land rights	- up to 50 years	straight-line basis																							
Buildings	- 30 to 60 years	straight-line basis																							
Distribution system	- 25 to 30 years	straight-line basis																							
General office equipment	- 10 years	straight-line basis																							
Computer equipment	- 5 years	straight-line basis																							
Computer software	- 3 years	straight-line basis																							
Rolling stock	- 5 to 8 years	straight-line basis																							
Other equipment	- 10 to 25 years	straight-line basis																							
Spare Transformers and Meters	<p>Spare transformers and meters are held to back up plant in service and are expected to substitute for original distribution plant transformers and meters when these original plant assets are being repaired.</p> <p>According to the criteria prescribed by the OEB in the AP Handbook the spare transformers and meters are treated as property, plant and equipment. Under Canadian GAAP for unregulated businesses the spare transformers and meters would be treated as inventory. In absence of rate regulation, inventory in 2006 would have been \$3,015,827 (2005 - \$2,733,850).</p>																								
Post 1999 Contributed Capital	Post 1999 contributed capital consists of third party contributions toward the cost of constructing distribution assets collected after January 1, 2000, and are recorded with property, plant and equipment as a contra account. Contributions are amortized at rates corresponding with the useful lives of the related property, plant and equipment. Canadian GAAP provides no specific guideline on the accounting for this type of contribution.																								

Barrie Hydro Distribution Inc.
Summary of Significant Accounting Policies

December 31, 2006

Construction in Progress	Construction in progress is comprised of the cost of assets not yet placed into service, assets under construction, and pre-construction activities related to projects expected to be completed. These amounts are not amortized. Upon completion of construction the amounts are transferred to property, plant and equipment and are amortized on a straight-line basis over the expected service life of the asset.
Long-term Investment	The corporation accounts for its investment by the cost method. Income from such investment is recognized only to the extent received or receivable.
Goodwill	<p>Goodwill represents the cost of acquired local distribution companies in excess of fair value of the net identifiable assets purchased.</p> <p>Goodwill is not amortized but is tested for impairment on an annual basis, or more frequently if events or changes in circumstances indicate that the asset might be impaired.</p> <p>Goodwill impairment is assessed based on a comparison for the fair value of the reporting unit to the underlying carrying value of the reporting unit's net assets, including goodwill.</p> <p>When the carrying amount of goodwill exceeds the implied fair value of goodwill an impairment loss is recognized in an amount equal to the excess as a charge against the results of operations.</p> <p>The corporation has determined that goodwill is not impaired.</p>
Deferred Charges	<p>Deferred financing charges represent the unamortized cost to issue long-term debt including fees paid to fix the interest rate of the issue. Amortization is provided on a straight-line basis, over the period to maturity of the related debt.</p> <p>Deferred separation charges represent an unamortized cost to purchase assets from Ontario Hydro Corporation in 1992. Amortization is provided on a straight-line basis, over the remaining useful life of the related assets of 16 years.</p>
Other Long-Term Assets	Other long-term assets consist of amounts paid to Hydro One under capital cost recovery agreements. These costs are amortized over the life of the agreements, being 25 years, which represents the guaranteed revenue stream for Hydro One.

Barrie Hydro Distribution Inc. Summary of Significant Accounting Policies

December 31, 2006

Regulatory Assets and Liabilities

The corporation has adopted the CICA's Accounting Guideline 19 "Disclosures by Entities Subject to Rate Regulation". Based on OEB regulations, certain costs and variance account balances are recorded regulatory assets or regulatory liabilities and are reflected in the balance sheet until the OEB determines the manner and timing of their disposition.

Regulatory assets represent future revenues associated with certain costs, incurred in current or prior period(s), that are expected to be recovered through the rate setting process. Regulatory assets and liabilities can arise from differences in amounts billed to customers (based on regulated rates) and the corresponding cost of non-competitive electricity service incurred by the corporation in the wholesale market administered by the Independent Electricity System Operator "IESO" after May 1, 2002. These amounts have been accumulated pursuant to regulation underlying the Electricity Act and deferred in anticipation of their future recovery in electricity distribution service charges.

Customer Deposits

Customer deposits represent amounts collected from customers to guarantee the payment of energy bills. The customer deposits liability includes interest credited to customers' deposit accounts, with interest expense recorded to offset this amount. Deposits expected to be refunded to customers within one year are classified as a current liability.

Customer deposits also include prudential deposits from retailers.

Construction Deposits

Construction deposits represent maintenance deposits and deposits for recoverable work.

Pension Plan

The corporation offers a pension plan for its full-time employees through the Ontario Municipal Employee Retirement System ("OMERS"). OMERS is a multi-employer, contributory, public sector pension fund established for employees of municipalities, local boards and school boards in Ontario. Participating employers and employees are required to make plan contributions based on participating employees' contributory earnings. The corporation accounts for its participation in OMERS as a defined contribution plan and recognizes the expense related to this plan as contributions are made.

Barrie Hydro Distribution Inc. Summary of Significant Accounting Policies

December 31, 2006

Post-employment Benefits

Employee future benefits other than pension provided by the corporation include medical and insurance benefits. These benefit plans provide benefits to certain employees when they are no longer providing active service.

Standards issued by The Canadian Institute of Chartered Accountants require the corporation to accrue for its obligations under other employee benefit plans and related costs.

The cost of post-employment benefits offered to employees are actuarially determined using the projected benefit method, prorated on service and based on assumptions that reflect management's best estimate. Under this method, the projected post-retirement benefit is deemed to be earned on pro-rata basis over the years of service in the attribution period commencing at date of hire, and ending at the earliest age the employee could retire and qualify for benefits.

The current service cost for the period is equal to the actuarial present value of benefits attributed to employees' services rendered in the period.

Past service costs from plan amendments are amortized on a straight-line basis over the average remaining service period of the employees active at the date of the amendment.

The excess of the net actuarial gains (losses) over 10% of the accrued benefit obligation are amortized into expense on a straight-line basis over the average remaining service period of active employees to full eligibility.

Subdivision Deposits

Subdivision deposits represent deposits received from developers based on the expected cost of capital for a new development. Once a year, the developer can request that an economic evaluation be performed based on the number of services connected during the year. A software developed by the EDA is used to determine the Economic Evaluation (Guidelines were created by OEB). The economic evaluation is a calculation of the net present value (NPV) of the expected revenue net of expected maintenance costs for the next 25 years. If the NPV calculation results in an amount less than the total cost to put the capital in place to service the subdivision the developer only receives a portion of their deposit back.

There is a 5 year window for the developer to collect any refunds available to them. If the money is not refunded to the developer it will be recorded as post 1999 contributed capital and taken out of the subdivision rebate account.

Barrie Hydro Distribution Inc. Summary of Significant Accounting Policies

December 31, 2006

Subdivision Deposits continued

The OEB has stated that effective January 1, 2007 an economic evaluation is to be done at the beginning of the process and funds received will be based on developers anticipated share of the cost based on the NPV calculation.

Revenue Recognition

Revenue from the sale and distribution of electricity is recognized on the accrual basis. The revenue includes cycles billed during the year plus an estimate for unbilled revenue. The unbilled revenue is calculated by estimating the consumption of electricity by customers since their last meter reading date to December 31, 2006. Actual results could differ from estimates made of electricity usage.

Other revenues, which include revenues from pole attachment, customer demand work, and other miscellaneous revenues are recognized at the time the service is provided.

Payment in Lieu of Corporate

Income Taxes and Capital Taxes

The corporation is a municipal electricity utility ("MEU") for purposes of the PIL's regime contained in the Electricity Act, 1998. As a MEU the corporation is exempt from tax under the Income Tax Act (Canada) and the Corporations Tax Act (Ontario).

Each taxation year, the corporation is required to make payments in lieu of corporate income taxes and capital taxes to Ontario Electricity Financial Corporation ("OEFC"). These payments are calculated based on the rules for computing taxable income and taxable capital outlined in Income Tax Act (Canada) and the Corporations Tax Act (Ontario) with taking into account any modifications made by the Electricity Act, 1998, and related regulations.

The corporation provides for payments in lieu of corporate income taxes and capital taxes related to its regulated business using the taxes payable method as permitted by the CICA and the OEB.

Under this method, no provisions are made for future income taxes as a result of temporary differences between the tax bases of assets and liabilities and their carrying amounts for accounting purposes. When unrecorded future income taxes become payable or receivable, it is expected that they will be reflected in the rates approved by the OEB at that point in time.

Barrie Hydro Distribution Inc. Summary of Significant Accounting Policies

December 31, 2006

Use of Estimates and Measurement Uncertainty

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes as well as the disclosure of contingent assets and liabilities at the financial statement date.

Accounts receivable, unbilled revenue, regulatory assets, regulatory liabilities and employee future benefits are reported based on amounts expected to be recovered or incurred and an appropriate allowance has been provided based on management's estimate of unrecoverable amounts.

Due to uncertainty involved in making such estimates, actual results could differ from those estimates, including changes as a result of future decisions made by the OEB, the Minister of Energy or the Minister of Finance.

The financial statements have, in management's opinion, been properly prepared using careful judgment within reasonable limits of materiality and within the framework of the accounting policies.

Financial Instruments

The corporation carries various forms of financial instruments. Unless otherwise noted, it is management's opinion that the corporation 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.

Barrie Hydro Distribution Inc.
Notes to Financial Statements

For the year ended December 31, 2006

1. Cash

The corporation's bank accounts are held at one chartered bank. The corporation received interest on the bank accounts at prime less 2% until April of 2006 at which time the rate was changed to prime less 1.75%.

2. Property, Plant and Equipment and Construction in Progress

	2006		2005	
	Cost	Accumulated Amortization	Cost	Accumulated Amortization
Land	\$ 1,856,641	\$ -	\$ 1,856,641	\$ -
Land rights	75,274	57,926	75,274	56,589
Buildings	17,303,742	4,080,073	16,671,546	3,729,083
Distribution system	192,050,087	73,846,958	175,738,482	66,857,593
Spare meters and transformers	1,493,009	-	1,440,068	-
General office equipment	1,276,900	1,037,239	1,275,362	995,335
Computer equipment	5,189,734	3,468,322	4,916,036	2,906,308
Computer software	2,986,562	1,827,031	2,373,102	1,153,873
Rolling stock	3,878,133	2,716,647	3,372,870	2,438,569
Other equipment	5,270,612	2,360,772	4,767,176	2,153,004
Post 1999 contributed capital	(22,319,787)	(2,636,181)	(18,909,541)	(1,878,200)
	\$209,060,907	\$ 86,758,787	\$193,577,016	\$ 78,412,154
Net Book Value		\$122,302,120		\$115,164,862

During the year the corporation acquired \$12,161,883 (2005 - \$7,467,407) of property, plant and equipment using cash.

	2006	2005
Construction in progress	\$ 2,420,821	\$ 4,033,601

Barrie Hydro Distribution Inc.
Notes to Financial Statements

For the year ended December 31, 2006

3. Long-term investment

	2006	2005
3.5784% interest in the ENERconnect Limited Partnership	\$ 71,785	\$ 71,785

The fair value of the ENERconnect Limited Partnership is not readily determinable as it is not a publicly traded investment.

4. Deferred Charges and Other Long-term Assets

	2006	2005
Separation charges	\$ 12,444	24,888
Financing costs	307,760	453,680
Deferred assets - Hydro One	738,483	451,025
	\$ 1,058,687	929,593

During the year the corporation entered into an agreement with Hydro One for the right to use meters. The total cost per the agreement was \$314,862. The asset is being amortized over the term of the agreement of 25 years.

Amortization of the separation charges in the amount of \$12,444 (2005 - \$12,444), financing fees in the amount of \$145,920 (2005 - \$275,920), and deferred assets - Hydro One in the amount of \$27,404 (2005 - \$19,007) are included in the Statement of Operations and Retained Earnings.

5. Regulatory Assets and Liabilities

Regulatory assets and liabilities arise as a result of the rate-making process and consist of the following:

	2006	2005
Retail settlement variance accounts	\$ (1,529,885)	\$ 5,467,559
Smart meters deferred revenue	(110,240)	-
Net carrying charges calculated at OEB specified rate	723,406	724,007
Recovery of regulatory assets	(741,050)	(4,327,223)
Net Regulatory Assets (Regulatory Liabilities)	\$ (1,657,769)	\$ 1,864,343

Barrie Hydro Distribution Inc.
Notes to Financial Statements

For the year ended December 31, 2006

5. Regulatory Assets and Liabilities continued

Regulatory balances are comprised as follows:

(i) Settlement Variances:

Settlement variances represent the differences between amounts charged by the corporation to its' customers based on regulated rates and the corresponding cost incurred by the corporation in the wholesale market administered by the IESO. Under the OEB's direction, the corporation has deferred the settlement variances that have occurred since May 1, 2002. Accordingly, the corporation has deferred these recoveries in accordance with the AP Handbook.

The OEB allows the variances to be deferred which would normally be recorded as revenue for unregulated businesses under Canadian GAAP. In absence of rate regulation, revenues in 2006 would have been \$3,522,112 higher (2005 - \$1,305,245 higher). The deferred balance for unapproved settlement variances continues to be calculated and carrying charges are accumulated in accordance with the OEB's direction. The manner and timing of disposition of the variance has not been determined by the OEB.

(ii) Carrying Charges

Carrying charges are calculated monthly on the opening balance of the applicable variance account using a specific interest rate as outlined by the OEB. In the absence of rate regulation, other revenues would have been higher by \$601 (2005 - \$98,357 lower).

(iii) Recovery of Regulatory Assets

In a letter dated December 19, 2003, the Minister of Energy granted approval for distributors to make application to the OEB with regard to rate recovery of certain distribution regulatory assets whose inclusion in rates was delayed by the Electricity Pricing, Conservation and Supply Act, 2002 (Electric Pricing, Conservation and Supply Act). As a result of the corporation's distribution rate application dated January 22, 2004, the distribution regulatory assets that accumulated up to December 31, 2002 are expected to be recovered over a four-year period, effective March 1, 2004 with an implementation date for consumption of April 1, 2004.

The rate application for 2006, approved by the OEB, included the recovery of regulatory assets accumulated to December 31, 2004 plus projected interest on these balances up to April 30, 2006. This second phase of recovery is for a two year period with rates effective May 1, 2006.

(iv) Additional Information

Included in regulatory assets is \$265,526 to reflect amounts owing to Hydro One with respect to low voltage charges relating to the time period beginning May 1, 2002 ending December 31, 2003. Also included in regulatory assets is \$123,248 representing an estimate of the low voltage charges for the period beginning January 1, 2004 ending April 30, 2006. These amounts was included in the rate submission for 2006 and is being recovered over a two year period through rates effective May 1, 2006.

Under the OEB's direction all regulatory asset balances as at December 31, 2004 plus accrued interest up to April 30, 2006 were applied against the regulatory asset recovery account. The result of this was a decrease in the settlement variances accounts of \$4,919,561 and a decrease in the carrying charges of \$1,139,033.

Barrie Hydro Distribution Inc.
Notes to Financial Statements

For the year ended December 31, 2006

5. Regulatory Assets and Liabilities continued

(v) Fair Value of Regulatory Assets and Regulatory Liabilities

For certain regulatory items identified above, the expected recovery or settlement period, or likelihood of recovery or settlement, is affected by risks and uncertainties related to the ultimate authority of the regulator in determining the asset's treatment for rate setting purposes.

Management continually assesses the likelihood of recovery of regulatory assets. If recovery through future rates is no longer considered probable, the amounts would be charged to the results of operations in the period that the assessment is made.

6. Related Party Transactions

The Corporation of the City of Barrie is the 100% owner of Barrie Hydro Holdings Inc. which is the parent company of Barrie Hydro Distribution Inc. and Barrie Hydro Energy Services Inc.

At the end of the year, the amounts due to related parties are as follows:

	<u>2006</u>	<u>2005</u>
The Corporation of the City of Barrie	\$ 750,468	\$ 1,158,305
Barrie Hydro Energy Services Inc.	151,171	259,319
Barrie Hydro Holdings Inc.	1,526,882	1,731,403
	<u>\$ 2,428,521</u>	<u>3,149,027</u>

These balances are interest-free, payable on demand and have arisen from the sales of product and provision of services referred to below.

Included in the amount due to Barrie Hydro Holdings Inc. is a dividend payable of \$1,450,000 (2005 - \$1,650,000) (see Note 15).

The corporation is also indebted to the Corporation of the City of Barrie for a \$20,000,000 (2005 - \$20,000,000) promissory note (see Note 9).

Barrie Hydro Distribution Inc.
Notes to Financial Statements

For the year ended December 31, 2006

6. Related Party Transactions - continued

The following are the corporation's related party transactions for the year:

During the year, the corporation billed electricity and services to the Corporation of the City of Barrie in the amount of \$1,508,471 (2005 - \$1,459,009).

During the year, the corporation billed miscellaneous revenues to the Corporation of the City of Barrie in the amount of \$1,160,946 (2005 - \$1,113,858).

During the year, the corporation paid municipal taxes to the Corporation of the City of Barrie in the amount of \$303,753 (2005 - \$295,784). Municipal taxes are included in administration and general on the Statement of Operations and Retained Earnings.

During the year, the corporation was charged interest expense of \$1,300,008 (2005 - \$1,612,500) by the Corporation of the City of Barrie.

Barrie Hydro Distribution Inc. invoiced Barrie Hydro Energy Services Inc. an amount of \$1,480,731 (2005 - \$1,411,216) for billing and collection services.

These transactions are in the normal course of operations and are measured at fair value.

7. Other Long-term Liabilities

	<u>2006</u>		<u>2005</u>
Developer deposits	\$ 111,207	\$	141,207
Collateral funds	132,907		<u>127,774</u>
	\$ 244,114	\$	268,981

Collateral funds represent amounts collected in lieu of development charges. Use of these funds is limited to specific terms set out in an agreement. The above balance includes accrued interest calculated annually at a rate equal to the bank rate obtained by the Corporation for its deposits.

**Barrie Hydro Distribution Inc.
Notes to Financial Statements**

For the year ended December 31, 2006

8. Employee Future Benefits

Barrie Hydro Distribution Inc. pays certain medical and insurance benefits under an unfunded defined benefit plan on behalf of its retired employees. The corporation recognizes these post-retirement costs in the period in which the employees render the services.

An actuarial report was performed and dated February 17, 2005. The accrued benefit obligation and current service cost were determined using the projected method, pro-rated on service. The actuarial valuation was performed on the post-retirement obligations sponsored by Barrie Hydro Distribution Inc. as at January 1, 2004. The next actuarial valuation will be performed in 2007.

Information about Barrie Hydro Distribution Inc.'s defined benefit plan is as follows:

	<u>2006</u>	<u>2005</u>
Accrued benefit obligation, opening balance	\$ 2,371,626	\$ 2,171,622
Current service cost	72,701	68,910
Interest cost	127,382	121,096
Actuarial losses	81,447	87,568
Benefits paid	<u>(81,448)</u>	<u>(77,570)</u>

Projected accrued benefit obligation at December 31, 2006 using a 5.5% discount rate	<u>\$ 2,571,708</u>	<u>\$ 2,371,626</u>
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Unfunded accrued benefit obligation	<u>\$ 2,571,708</u>	<u>\$ 2,371,626</u>
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Additional Disclosures:

Unamortized actuarial gain (loss)	<u>\$ -</u>	<u>\$ -</u>
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Sensitivity Analysis

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans.

The effect of a one-percentage point increase in assumed health care cost trend rates on 2006:

Accrued benefit obligation, end of period	<u>\$ 2,717,708</u>	<u>\$ 2,517,626</u>
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Increase in net period benefit cost	<u>\$ 146,000</u>	<u>\$ 146,000</u>
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The effect of a one-percentage point decrease in assumed health care cost trend rates on 2006:

Accrued benefit obligation, end of period	<u>\$ 2,447,708</u>	<u>\$ 2,247,626</u>
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Decrease in net period benefit cost	<u>\$ 124,000</u>	<u>\$ 124,000</u>
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Barrie Hydro Distribution Inc.
Notes to Financial Statements

For the year ended December 31, 2006

8. Employee Future Benefits - continued

The main actuarial assumptions employed for the valuations are as follows:

(a) General inflation:

Future general inflation levels, as measured by changes in the Consumer Price Index ("CPI"), were assumed at 2.2% in 2006 (2005 - 2.2%).

(b) Interest (discount) rate:

The obligation as at December 31, 2006, representing the present value of future liabilities was determined using a discount rate of 5.5% (2005 - 5.5%). This corresponds to the assumed CPI rate plus an assumed real rate of return of 3.3% (2005 - 3.3%).

(c) Salary levels:

Future general salary and wage levels were assumed to increase at 3.5% (2005 - 3.5%) per annum.

(d) Medical costs:

Medical costs were assumed to increase at the CPI rate plus a further increase of 6.8% (2005 - 7.8%). This rate will be graded down by 1% per year to 2.8% in 2009 and thereafter.

(e) Dental costs:

Dental costs were assumed to increase at the CPI rate plus a further increase of 2.8% (2005 - 2.8%).

Barrie Hydro Distribution Inc.
Notes to Financial Statements

For the year ended December 31, 2006

9. Long-term Debt

	2006	2005
6.45% EDFIN bond, with interest only payable in arrears semi-annually on August 15 and February 15, maturing August 15, 2012	\$ 25,000,000	\$ 25,000,000
6.5% unsecured promissory note, payable to the Corporation of the City of Barrie with interest only payable December 31 maturing December 31, 2007	20,000,000	20,000,000
	\$ 45,000,000	\$ 45,000,000

(a) EDFIN bond:

In August of 2002 the corporation refinanced part of the existing debt with a 10-year bond issue for \$25,000,000. The corporation was one of five local distribution companies ("LDCs") that participated in the Electricity Distributors Finance Corporation ("EDFIN") 10-year Bond issue (Series 2002-1) that was offered on a private placement. EDFIN is a special purpose corporation managed by MEARIE Management Inc., for the purpose of providing LDCs with efficient access to the debt capital markets. Each LDC has executed a debenture which is a direct and unsecured obligation of the LDC. The LDCs' obligations will be several and not joint, and each LDC will be liable for its own obligation and not that of any other LDC. Due to a change in structure of the participating corporations, there are now three LDCs with EDFIN bonds.

(b) Promissory note:

The \$20,000,000 was renewed in 2005 for a two-year term with the additional term commencing on January 1, 2006 with an interest rate of 6.5% per annum. The promissory note has not been reclassified to current liabilities as it is expected that it will be renewed or re-financed through another long-term debt facility.

10. Obligations Under Capital Lease

	2006	2005
Capital lease, \$3,648 payable monthly, bearing interest at 4.75%, maturing September 2008, secured by computer equipment, plus a \$21,903 buyout at the end of the term	\$ 94,740	\$ 133,264
Capital lease, \$1,249 payable monthly, bearing interest at 7.45%, maturing September 2008, secured by computer equipment	24,524	37,172
	119,264	170,436
Less amount due within one year included in current liabilities	(54,372)	(51,171)
	\$ 64,892	\$ 119,265

Barrie Hydro Distribution Inc.
Notes to Financial Statements

For the year ended December 31, 2006

10. Obligations Under Capital Lease continued

The future minimum lease payments are as follows:

2007	\$	58,764
2008		<u>65,975</u>
		124,739
less: Imputed interest		<u>(5,475)</u>
	\$	<u>119,264</u>

11. Pension Agreements

The corporation makes contributions to the OMERS, which is a multi-employer plan, on behalf of members of its 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. The plan is financed by equal contributions from participating employers and employees, and by the investment earnings of the fund.

The contribution rates for 2006 were 6.5% for employees earning up to \$43,700 and 9.6% thereafter. The amount contributed to OMERS for 2006 was \$487,969 (2005 - \$435,695).

12. Liability Insurance

The corporation belongs to the Municipal Electrical Reciprocal Insurance Exchange ("MEARIE"). MEARIE is a self-insurance plan that pools the risks of all of its members. Any losses experienced by MEARIE are shared amongst its members. As at December 31, 2006, the corporation has not been made aware of any assessments for losses.

Barrie Hydro Distribution Inc. Notes to Financial Statements

For the year ended December 31, 2006

13. Contingent Liabilities

i) Griffith et al. v. Toronto Hydro-Electric Commission et al.

This action has been brought under the Class Proceedings Act, 1992. The plaintiff class seeks \$500 million in restitution for amounts paid to Toronto Hydro and to other Ontario municipal electric utilities ("LDCs") who received late payment penalties which constitute interest at an effective rate in excess of 60% per year, contrary to section 347 of the Criminal Code. Pleadings have closed in this action. The action has not yet been certified as a class action and no discoveries have been held, as the parties were awaiting the outcome of a similar proceedings brought against Enbridge Gas Distribution Inc. (formerly Consumers Gas).

On April 22, 2004, the Supreme Court of Canada released a decision in the Consumers Gas case rejecting all of the defences which had been raised by Enbridge, although the Court did not permit the Plaintiff class to recover damages for any period prior to the issuance of the Statement of Claim in 1994 challenging the validity of late payment penalties. The Supreme Court remitted the matter back to the Ontario Superior Court of Justice for determination of the damages. At the end of 2006, a mediation process resulted in the settlement of the damages payable by Enbridge.

After the release by the Supreme Court of Canada of its 2004 decision in the Consumers Gas case, the plaintiffs in the LDC late payment penalties class action indicated their intention to proceed with their litigation against the LDCs. To date, no formal steps have been taken to move the action forward. The electric utilities intend to respond to the action if and when it proceeds on the basis that the LDCs' situation may be distinguishable from that of Consumers Gas.

The corporation collected total late payment penalties of approximately \$4,569,000 from April 30, 1994 to May 1, 2001. No determination of the portion of these payments which may have constituted interest at an impermissible rate has been made, and as such, no accrual for any potential liability has been recorded in the financial statements.

(ii) The corporation has other claims outstanding which in managements' opinion will be covered by insurance.

iii) The corporation has posted a letter of credit for \$100,000 maturing on October 31, 2007.

14. Share Capital

The corporation is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares.

The issued share capital is as follows:

	2006	2005
1,000 Common shares	<u>\$ 61,491,374</u>	<u>\$ 61,491,374</u>

Barrie Hydro Distribution Inc.
Notes to Financial Statements

For the year ended December 31, 2006

15. Dividends

During 2004 a dividend policy was adopted by the Board of Directors of Barrie Hydro Holdings Inc. stating that the amount of dividends payable by the corporation to the Corporation of the City of Barrie is equal to 30% of the corporation's audited net income after extraordinary items for the year.

Dividends totalling \$3,100,000 were paid during the 2006 fiscal year, which included management's best estimate of \$1,650,000 declared in 2005 plus \$82,900 declared in 2006 for the difference between the estimated 2005 dividend and the actual dividend based on the above mentioned policy. A one-time additional dividend of \$1,167,100 was approved by the Board and paid during the year. This extra dividend was issued to increase the dividend payment with respect to 2005 to 50% of net income. Furthermore, the Board approved and paid a dividend of \$200,000.

An additional \$1,450,000 dividend has been declared under the policy calculated using management's best estimate and has been accrued in these financial statements (see Note 6). The dividend is to be paid prior to June 30, 2007. Any difference between the dividend estimated for and the dividend calculated using the December 31, 2006 audited net income after extraordinary items will be paid in 2007.

The dividends reported on the statement of operations include the following dividends declared and described above \$82,900, \$1,167,100, \$200,000 and the \$1,450,000 for a total of \$2,900,000.

Barrie Hydro Distribution Inc.
Notes to Financial Statements

For the year ended December 31, 2006

16. Payments in Lieu of Corporate Income Taxes, Capital Taxes, Large Corporation Tax and Future Income Taxes

(a) Payments in lieu of corporate income taxes ("PILs"), large corporation tax and capital taxes

The corporation's provision for PILs is calculated as follows:

	<u>2006</u>	<u>2005</u>
Income before provision for PILs	\$ 9,935,905	\$ 10,476,784
Finance costs and employee benefits	154,642	283,934
Regulatory assets added back for tax purposes	3,522,112	1,269,246
Capital tax included in tax provision	(373,739)	(394,768)
Capital cost (greater than) less than amortization expense	246,976	(21,837)
Other items	38,779	(59,603)
	<u>13,524,675</u>	<u>11,553,756</u>
Income for tax purposes		
Statutory Canadian federal and provincial tax rate	36.12%	36.12%
	<u>4,885,113</u>	<u>4,172,773</u>
Provision for PILs		
Part I.3 tax on large corporations	-	12,732
Capital tax	373,739	394,768
Other	191,148	120,305
	<u>191,148</u>	<u>120,305</u>
Total provision	<u>\$ 5,450,000</u>	<u>\$ 4,700,578</u>

(b) Future Taxes

Future income taxes have not been recorded in the accounts as they are expected to be reflected through future distribution revenues.

Significant components of the corporation's future taxes are as follows:

	<u>2006</u>	<u>2005</u>
Employee future benefits	\$ 929,000	\$ 857,000
Regulatory assets and liabilities	599,000	(673,000)
Property, plant and equipment	8,776,000	9,235,000
	<u>8,776,000</u>	<u>9,235,000</u>
Net future income tax asset	<u>\$ 10,304,000</u>	<u>\$ 9,419,000</u>

A future income tax expense (recovery) of \$(885,000) (2005 - \$496,000) has not been reflected in the provision.

Barrie Hydro Distribution Inc.
Notes to Financial Statements

For the year ended December 31, 2006

17. Risk Management for Fair Value of Financial Assets and Liabilities

The fair value of the financial instruments included in the financial statements, other than the long-term investment, long-term debt and related party balances, approximate their carrying amount because of the short maturity of these instruments.

The fair value of the long-term investment is not readily determinable as it is not a publicly traded investment.

The carrying value of the debenture payable, included in long-term debt, in the amount of \$25,000,000 approximated its fair value as at December 31, 2006 based on quoted market prices.

The fair values of the corporation's related party note payable to the Corporation of the City of Barrie and other amounts due to/from related parties are not determinable due to their related party nature and terms.

The corporation is not exposed to significant interest rate risk as a result of the short-term maturity of its monetary current assets and current liabilities.

Financial assets held by the corporation expose it to credit risk. As at December 31, 2006 there were no significant concentrations of credit risk with respect to any class of financial assets.

18. Statement of Cash Flows

	<u>2006</u>	<u>2005</u>
Interest paid	<u>\$ 3,226,277</u>	<u>\$ 3,555,171</u>
Interest received	<u>\$ 215,453</u>	<u>\$ 117,437</u>
Payment in lieu of corporate income taxes, Part 1.3 and capital taxes paid (net of taxes received)	<u>\$ 5,392,443</u>	<u>\$ 5,916,146</u>

19. Comparative Amounts

Certain comparative figures presented in the financial statements for 2005 have been restated to conform to the financial statement presentation adopted for 2006.
