

Financial Statements of

CHATHAM-KENT HYDRO INC.

December 31, 2005

Management's Responsibility for Financial Reporting

Chatham-Kent Hydro's management is responsible for the preparation and presentation of the financial statements and all other information included in this annual report. Management is also responsible for the selection and use of accounting principles that are appropriate in the circumstances, and for the internal controls over the financial reporting process to reasonably ensure that relevant and reliable information is produced. Financial statements are not precise in nature as they include certain amounts based on estimates and judgement. Management has determined such amounts on a reasonable basis in order to ensure that the financial statements are presented fairly, in all material respects.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control over the financial reporting process. The Board exercises this responsibility through the Audit Committee of the Board. This committee, which is comprised of three directors of the Chatham-Kent Energy Board with one member also on the Chatham-Kent Hydro Board, meets with management and the external auditors to ensure that management responsibilities are properly discharged and to review the financial statements and other information included in the annual report before they are presented to the Board of Directors for approval. The financial statements have been approved by the Board of Directors on the recommendation of the Audit Committee.

Deloitte & Touche LLP, an independent firm of Chartered Accountants, has been appointed by the audit committee and engaged to examine the accompanying financial statements in accordance with generally accepted auditing standards in Canada and provide an independent professional opinion. Their report is presented with the financial statements.



Dave Kenney, President



Jim Hogan, Chief Financial & Regulatory Officer

Auditor's Report

To the Chairman and Board Members of Chatham-Kent Hydro Inc.

We have audited the balance sheet of Chatham-Kent Hydro Inc. as at December 31, 2005 and the statements of earnings and retained earnings and of 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.

A handwritten signature in black ink that reads "Deloitte Touche LLP". The signature is written in a cursive, flowing style.

Chartered Accountants

June 19, 2006

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CHATHAM-KENT HYDRO INC.

Balance Sheet

December 31, 2005

	2005	2004
ASSETS		
CURRENT		
Cash and cash equivalents	\$ 9,581,604	\$ 14,022,252
Accounts receivable (Note 3)	2,666,469	4,360,128
Accounts receivable – unbilled revenue	10,253,024	7,782,646
Due from Chatham-Kent Energy Inc.	1,600,000	-
Due from Middlesex Power Distribution Corporation	455,953	-
Inventories	573,348	566,961
Prepaid expenses	65,608	127,974
	25,196,006	26,859,961
CAPITAL ASSETS (Note 4)	40,657,412	40,014,768
OTHER		
Deferred assets (Note 5)	3,238,516	2,309,248
Computer software	5,995	9,928
	3,244,511	2,319,176
	\$ 69,097,929	\$ 69,193,905
LIABILITIES		
CURRENT		
Accounts payable and accrued liabilities	\$ 14,974,906	\$ 10,622,337
Taxes payable	291,111	149,781
Due to the Municipality of Chatham-Kent	1,812,626	3,476,752
Current portion of customers deposits	783,290	827,000
	17,861,933	15,075,870
LONG-TERM		
Note payable (Note 6)	23,523,326	23,523,326
Regulatory revenue payable	83,650	294,850
Provision for asset retirement obligation	30,000	39,000
Employee future benefits (Note 7)	723,535	672,678
Long-term portion of customer deposits	1,508,847	1,337,956
	25,869,358	25,867,810
	43,731,291	40,943,680
CONTINGENCY (Note 10)		
SHAREHOLDER'S EQUITY		
Share capital (Note 11)	23,523,425	23,523,425
Retained earnings	1,843,213	4,726,800
	25,366,638	28,250,225
	\$ 69,097,929	\$ 69,139,905

CHATHAM-KENT HYDRO INC.
Statement of Earnings and Retained Earnings
Year Ended December 31, 2005

	2005	2004
SERVICE REVENUE		
Residential	\$ 22,147,951	\$ 19,387,119
General service	46,683,479	41,445,387
Street lighting	689,417	633,592
	69,520,847	61,466,098
Change in unbilled revenue	2,158,620	640,184
	71,679,467	62,106,282
Retailer energy sales	11,419,852	9,036,548
Total Energy Sales	83,099,319	71,142,830
COST OF POWER	71,404,758	60,246,512
GROSS MARGIN ON SERVICE REVENUE	11,694,561	10,896,318
OTHER OPERATING REVENUE	1,336,837	1,242,272
OPERATING INCOME	13,031,398	12,138,590
OPERATING AND MAINTENANCE EXPENSE		
Distribution	2,486,511	2,522,647
ADMINISTRATIVE EXPENSE		
Billing and collection	1,404,972	1,477,513
General administration	1,424,946	1,332,124
Interest	1,726,279	1,696,875
DEPRECIATION AND AMORTIZATION	2,846,538	2,766,963
	9,889,246	9,796,122
EARNINGS BEFORE PAYMENTS IN LIEU OF TAXES	3,142,152	2,342,468
Payments in lieu of taxes (Note 14)	1,225,739	860,833
NET EARNINGS	1,916,413	1,481,585
RETAINED EARNINGS, BEGINNING OF YEAR	4,726,800	3,745,215
DIVIDENDS PAID	(4,800,000)	(500,000)
RETAINED EARNINGS, END OF YEAR	\$ 1,843,213	\$ 4,726,800

CHATHAM-KENT HYDRO INC.

Statement of Cash Flow

Year Ended December 31, 2005

	2005	2004
OPERATING ACTIVITIES		
Net earnings	\$ 1,916,413	\$ 1,481,585
Adjustments for:		
Depreciation of capital assets	3,120,526	3,032,393
Depreciation of computer software	3,933	3,433
Amortization of contributed capital	(116,101)	(111,355)
Allowance for deferred assets	(339,000)	(300,000)
Gain on disposal of capital assets	(83,930)	(103,666)
Provision for asset retirement obligation	(9,000)	39,000
Employee future benefits	50,857	63,465
Changes in non-cash working capital items (Note 12)	1,609,370	3,606,693
Changes in long-term customer deposits	170,891	(269,178)
	6,323,959	7,442,370
INVESTING ACTIVITIES		
Additions to deferred assets	(1,902,024)	(637,250)
Recovery of deferred assets	1,311,756	380,942
Regulatory revenue payable	(211,200)	54,850
Proceeds on disposal of capital assets	113,330	124,984
Additions to capital assets and computer software	(3,676,469)	(3,599,841)
Due from Chatham-Kent Energy Inc.	(1,600,000)	(2,659)
	(5,964,607)	(3,678,974)
FINANCING ACTIVITIES		
Dividends	(4,800,000)	(500,000)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(4,440,648)	3,263,396
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	14,022,252	10,758,856
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 9,581,604	\$ 14,022,252

See Note 12 for supplemental cash flow information.

CHATHAM-KENT HYDRO INC.
Notes to the Financial Statements
December 31, 2005

1. NATURE OF OPERATIONS

(a) *Incorporation of Chatham-Kent Hydro Inc.*

Chatham-Kent Hydro Inc. (“the Company”) was incorporated September 22, 2000 under the *Business Corporations Act (Ontario)*.

The Company is wholly-owned by Chatham-Kent Energy Inc. which in turn is wholly-owned by the Municipality of Chatham-Kent (“the Municipality”).

The principal activity of the Company is to distribute electricity to customers within the Municipality of Chatham-Kent, under the license issued by the Ontario Energy Board (“OEB”).

Under a Municipal by-law, dated September 5, 2000, the former Public Utilities Commission of the Municipality of Chatham-Kent – Electrical Division (“the Commission”) and the Municipality transferred the assets, liabilities and employees associated with the distribution of electricity at book value effective October 1, 2000. The book value of the net assets transferred to the Company at October 1, 2000 was \$47,046,751. In consideration for the transfer the company issued long-term notes payable to the Municipality in the aggregate principal amount of \$23,523,326. Shares valued at \$23,523,425 have been issued to Chatham-Kent Energy Inc.

The incorporation and subsequent reorganization was required by provisions of Bill 35, *The Energy Competition Act, 1998* enacted by the Province of Ontario to introduce competition in the electricity market.

(b) *Rate Regulated Entity*

OEB

The Company is a regulated electricity Local Distribution Company (LDC) and has a distribution licence that is regulated by the OEB. The OEB has regulatory oversight of electricity matters in Ontario. *The Ontario Energy Board Act, 1998* sets out the OEB’s authority to issue a distribution licence which must be obtained by owners or operators of a distribution system in Ontario. The OEB prescribes licence requirements and conditions including, among other things, specified accounting records, regulatory accounting principles and filing process requirements for rate-setting purposes.

The OEB’s authority and responsibilities include the power to approve and fix rates for the transmission and distribution of electricity, the power to provide continued rate protection for rural and remote electricity customers and the responsibility of ensuring the electricity distribution companies fulfill obligations to connect and service customers.

CHATHAM-KENT HYDRO INC.

Notes to the Financial Statements

December 31, 2005

1. NATURE OF OPERATIONS (continued)

The Company is required to charge its customers for the following amounts (all of which, other than the distribution rates, represent a pass through of amounts payable to third parties):

- Electricity Price – The electricity price represents the commodity cost of electricity.
- Distribution Rate – The distribution rate is designed to recover the costs incurred by the Company in delivering electricity to customers and the OEB allowed rate of return.
- Retail Transmission Rate – The retail transmission rate represents the wholesale costs incurred by Company in respect of the transmission of electricity from generating stations to the local areas.
- Wholesale Market Service Charge – The wholesale market service charge represents the various wholesale market support costs.

In order to operate in the Ontario electrical industry all market participants, including the Company, are required to satisfy and maintain prudential requirements with the Independent Electricity System Operator (“IESO”), which include credit support with respect to outstanding market obligations in the form of obtaining a credit rating, letters of credit, cash deposits or guarantees from third parties with prescribed credit ratings.

Market Based Rate of Return

The OEB regulates the rates of the Company in a cost-of-service regime. A part of the cost-of-service rate setting is the market based rate of return which the OEB has approved the maximum rate to be 9.88%. The Company however elected to apply for a rate of return of 6.05% in the initial rate setting in 2001.

The initial rate setting process of 2001 required a three year phase-in of the rate change to minimize the impacts to the customers. The final implementation of the rates occurred in April 2005 for \$1,000,000 however the Company is required to invest the same amount of funds in Conservation and Demand Management programs between May 2005 and September 2007.

The next rate rebasing is scheduled for May 2006 which will update the market based rate of return as well as set rates on the 2004 rate base.

Regulatory Assets and Liabilities

Electricity distributors are required to reflect certain prescribed costs on their balance sheet until the manner and timing of distribution is determined by the OEB. These costs are: transition costs resulting from preparation to Open Access; settlement variances between amounts charged by the Company to customers (based on regulated rates) and corresponding cost of non-competitive electricity service incurred by it in the wholesale market administered by the IESO after May 1, 2002; the deferral of OEB annual cost assessments for the OEB’s fiscal year 2004 and subsequent fiscal years; and the deferral of incremental Ontario Municipal Employees Retirement System pension expenditures for fiscal years starting after January 1, 2005.

CHATHAM-KENT HYDRO INC.

Notes to the Financial Statements

December 31, 2005

1. NATURE OF OPERATIONS (continued)

The regulatory assets and liabilities balances are detailed in Note 5. The regulatory assets have been recovered in rates on an interim basis since April 2004 over a four year period. Final prudence review and decision for full recovery is expected to be provided by the OEB in May 2006. The Company has a low cost per customer for the regulatory asset accounts thereby reducing the risk of not receiving OEB approval for recovering the amounts from customers.

2. SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared in accordance with Canadian generally accepted accounting principles and reflect the following policies as set forth in the Accounting Procedures Handbook issued by the OEB under the authority of the *Ontario Energy Board Act, 1998*:

Regulation

The company is regulated by the OEB and any power rate adjustments require OEB approval.

Inventories

Inventories are valued at the lower of cost and replacement cost with cost being determined using the weighted average method.

Capital assets

Capital assets are recorded at cost. Depreciation is calculated on a straight-line basis over the useful life as follows:

Buildings and fixtures	25 – 50 years
Distribution station equipment	30 years
Distribution lines	25 years
Distribution transformers	25 years
Distribution meters	25 years
General office equipment	10 years
Computer equipment	5 years
Rolling stock	4 – 8 years
Tools	10 years
System supervisory equipment	15 years
Automated mapping facility management	15 years
Services	25 years
Contributions in aid of construction	25 years

Computer software

Computer software is stated at cost less accumulated depreciation. It is depreciated over 5 years on a straight-line basis.

CHATHAM-KENT HYDRO INC.
Notes to the Financial Statements
December 31, 2005

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of long-lived assets

Long-lived assets are tested for recoverability whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. An impairment loss is recognized when their carrying value exceeds the total undiscounted cash flows expected from their use and eventual disposition. The amount of the impairment loss is determined as the excess of the carrying value of the asset over its fair value.

Asset retirement obligations

The Company recognizes the liability for an asset retirement that results from the acquisition, construction, development or normal operations. The liability for an asset retirement is initially recorded at its fair value in the year in which it is incurred and when a reasonable estimate of fair value can be made. The corresponding cost is capitalized as part of the related asset and is amortized over the asset's useful life. In subsequent years the liability is adjusted for changes resulting from the passage of time and revisions to either the timing or the amount of the original estimate of the undiscounted cash flows. The accretion of the liability to its fair value as a result of the passage of time is charged to earnings.

Deferred assets

Deferred assets consist of qualifying capital costs and related expenditures incurred in the preparation for market opening. Deferred assets also include costs for conservation programs which meet the Minister of Energy's Directive. Recovery of the deferred assets is regulated by the OEB.

Contributions in aid of construction

Contributions in aid of construction consist of third party contributions toward the cost of constructing Company assets. For the year ended December 31, 2005, \$118,719 (2004 - \$557,404) of contributed capital has been charged to capital assets and recorded as an offset to capital assets. Amortization is on a straight-line basis over 25 years.

Customer deposits

Customer deposits are recorded when paid. Deposits earn interest at a rate of prime less 2%.

Revenue recognition and cost of power

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 year. The related cost of power is recorded on the basis of power used. Any discrepancies in the revenue collected and associated cost of power related to distribution are charged to deferred assets.

CHATHAM-KENT HYDRO INC.
Notes to the Financial Statements
December 31, 2005

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Unbilled Revenue

Unbilled revenue is an estimate of customers' consumption of power from the last meter read to December 31st.

Use of 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 disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual result could differ from those estimates.

Post employment benefits other than pension

The Company provides its current and retired employees with life insurance and medical benefits beyond those provided by government-sponsored plans. The cost of these benefits is expensed as earned through employment service.

Payments in lieu of income taxes

Under the *Electricity Act, 1998*, the Company is required to make payments-in-lieu of corporate taxes to the Ontario Electricity Financial Corporation (OEFC). These payments are recorded 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)* and modified by the *Electricity Act, 1998*, and related regulations.

The Company, regulated by the Ontario Energy Board, provides for payments-in-lieu of corporate income taxes using the taxes payable method instead of the liability 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 for accounting purposes. Future income taxes are expected to be reflected in future rates and, accordingly, are not recognized in the financial information. Payment in lieu of taxes is henceforth referred to as income taxes.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand and balances with the bank.

CHATHAM-KENT HYDRO INC.
Notes to the Financial Statements
December 31, 2005

3. ACCOUNTS RECEIVABLE

	<u>2005</u>	<u>2004</u>
Electrical energy	\$ 2,523,267	\$ 3,383,332
Other	244,383	1,111,763
	<u>2,767,650</u>	4,495,095
Allowance for doubtful accounts	<u>(101,181)</u>	(134,967)
Net accounts receivable	<u>\$ 2,666,469</u>	\$ 4,360,128

4. CAPITAL ASSETS

	<u>2005</u>		<u>2004</u>	
	Cost	Accumulated Depreciation	Net Book Value	Net Book Value
Plant and distribution system:				
Land	\$ 386,825	\$ -	\$ 386,825	\$ 389,046
Buildings and fixtures	3,454,409	496,365	2,958,044	2,694,536
Distribution station equipment	199,845	67,659	132,186	144,672
Station retirement obligation	35,009	5,009	30,000	39,000
Distribution system:				
Overhead	18,893,014	4,448,319	14,444,695	14,185,678
Underground	13,811,406	3,730,640	10,080,766	10,161,457
Transformers	11,858,568	2,966,385	8,892,183	8,816,713
Meters	2,809,363	748,884	2,060,479	2,111,054
General office equipment	91,964	49,112	42,852	48,228
Computer equipment	333,567	276,813	56,754	86,399
Rolling stock	1,754,146	1,071,380	682,766	646,949
Tools	526,281	387,401	138,880	165,928
System supervisory equipment	653,619	361,159	292,460	313,305
Automated mapping facility	1,440,321	486,184	954,137	958,279
Services	2,273,554	299,657	1,973,897	1,720,417
	<u>58,521,891</u>	<u>15,394,967</u>	<u>43,126,924</u>	42,481,662
Contributions in aid of construction	<u>(2,885,841)</u>	416,329	<u>(2,469,512)</u>	(2,466,894)
	<u>\$ 55,636,050</u>	<u>\$14,978,638</u>	<u>\$ 40,657,412</u>	\$ 40,014,768

Depreciation and amortization in the amount of \$161,820 (2004 - \$157,506) for rolling stock and computer software is included with relevant cost centres.

CHATHAM-KENT HYDRO INC.
Notes to the Financial Statements
December 31, 2005

5. DEFERRED ASSETS

Deferred assets and liabilities arise as a result of the rate-making process. As described in this note, Chatham-Kent Hydro has recorded the following regulatory assets and provision.

	<u>2005</u>	<u>2004</u>
Transition costs	\$ 1,306,176	\$ 1,118,539
Retail settlement variance accounts	3,033,177	2,122,093
Conservation and demand management costs	679,460	296,136
Other deferred costs	419,979	-
Gross deferred assets	5,438,792	3,536,768
Recoveries		
Transition / RSVA	(969,368)	(380,942)
Conservation and demand management	(723,330)	-
Provision	(507,578)	(846,578)
Net deferred assets	\$ 3,238,516	\$ 2,309,248

The introduction of Bill 210 in November 2002 has deferred future rate increases until 2006. However Bill 4 was introduced in December 2003 which allowed for the recovery of deferred assets over a four year period beginning in April 2004. Deferred asset revenue for 2005 was \$588,426 (2004 - \$380,942). Since the recovery of the regulatory assets has begun the provision has been reduced by \$339,000 (2004 - \$300,000). While it continues to be management's intention to pursue future rate increases based on all of these costs and the related interest, they have provided an allowance of \$507,578 (2004 - \$846,578) for costs which may be disallowed for OEB purposes.

The Company incurred costs for Conservation and demand management for 2005 of \$383,324 (2004 - \$296,136). These costs are required in order to obtain the rate approval that was effective May 2005. The revenue received in 2005 was \$723,330 (2004 - \$Nil). The Company is required to invest \$1,000,000 by the end of September 2007.

6. NOTE PAYABLE

The note payable is due to the Municipality with no set repayment terms and interest payable monthly at 7.04 %. Interest expense for the year amounted to \$1,654,320 (2004 - \$1,654,320).

CHATHAM-KENT HYDRO INC.
Notes to the Financial Statements
December 31, 2005

7. EMPLOYEE FUTURE BENEFITS

The company pays certain medical and life insurance benefits on behalf of its current employees. The accrued benefit liability at December 31, 2005 was \$723,535 (2004 - \$672,678).

Information about the Company's defined benefit plan is as follows:

	<u>2005</u>	<u>2004</u>
Accrued benefit liability, beginning of year	\$ 672,678	\$ 609,213
Expense for the year	50,857	63,465
Estimated accrued benefit liability as at December 31.	<u>\$ 723,535</u>	<u>\$ 672,678</u>

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

General inflation

Future inflation levels, as measured by changes in the Consumers Price Index ("CPI"), were assumed to be 2.5% in 2004 and thereafter.

Interest (discount) rate

The present value of the future benefits and the expense for the year ended December 31, 2005 was determined using a discount rate of 5.75% (2004-5.75%). This corresponds to the assumed CPI rate plus an assumed rate of return of 2.5%.

Health costs

Health costs were assumed to increase at 10% per year for 10 years, and then at the CPI rate plus 1% thereafter.

Dental costs

Dental costs were assumed to increase at the CPI rate plus 1% for 2004 and thereafter.

Salary growth rate

Salary growth rate was assumed to increase at a rate of 3.5% for 2004 and thereafter.

CHATHAM-KENT HYDRO INC.

Notes to the Financial Statements

December 31, 2005

8. PENSION AGREEMENT

The Company provides a pension plan for its employees through the Ontario Municipal Employees' Retirement System ("OMERS"). OMERS is a multi-employer pension plan which operates as the Ontario Municipal Employees Retirement Fund ("the Fund") and provides pensions for employees of Ontario municipalities, local boards, public utilities, and school boards. The Fund is a contributory defined benefit pension plan, which is financed by equal contributions from participating employers and employees, and by the investment earnings of the Fund. As there is insufficient information to apply defined benefit plan accounting, defined contribution plan accounting has been used by the Company. The Company's contribution for employees' current service in 2005 was \$167,152 (2004 - \$154,633).

9. RELATED PARTY TRANSACTIONS

The Company provided the following services in the normal course of operations to the Municipality of Chatham-Kent:

	<u>2005</u>	<u>2004</u>
Energy (at commercial rates)	\$ 3,756,022	\$ 3,735,017
Streetlight maintenance	156,161	148,084
Capital for Bloomfield Park	-	154,839
	<u>\$ 3,912,183</u>	<u>\$ 4,037,940</u>

Chatham-Kent Utility Services Inc. provided the following services in the normal course of operations to the Company:

	<u>2005</u>	<u>2004</u>
Administrative services		
Billing, collecting & administrative services	\$ 2,870,981	\$ 2,730,455

Included in the costs above are deferred costs of \$114,469 (2004 - \$45,744) that are reflected on the balance sheet.

10. CONTINGENCY

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 the 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 states that late payment penalties result in the municipal electric 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 defense of this class action. At this time it is not possible to quantify the effect, if any, on the financial statements of the Company, and as such no potential liability has been recognized.

CHATHAM-KENT HYDRO INC.
Notes to the Financial Statements
December 31, 2005

11. SHARE CAPITAL

	<u>2005</u>	<u>2004</u>
Authorized		
Unlimited common shares		
Issued		
2,000 common shares	\$ 23,523,425	\$ 23,523,425

12. SUPPLEMENTAL CASH FLOW INFORMATION

Changes in non-cash working capital items

	<u>2005</u>	<u>2004</u>
Accounts receivable	\$ 1,693,659	\$ (504,738)
Accounts receivable – unbilled revenue	(2,470,378)	(742,091)
Due from Chatham-Kent Utility Services	-	32,447
Inventories	(6,387)	63,844
Prepaid expenses	62,366	(5,624)
Due from Middlesex Power Distribution Corporation	(455,953)	-
Due to Municipality of Chatham-Kent	(1,664,126)	3,236,306
Accounts payable and accrued liabilities	4,352,569	1,796,666
Taxes receivable/payable	141,330	(722,117)
Increase in current portion of customer deposits	(43,710)	452,000
	\$ 1,609,370	\$ 3,606,693

Payments in lieu of taxes of \$1,112,232 (2004 - \$1,583,000) and interest of \$1,726,279 (2004 - \$1,696,875) were paid during the year.

13. FINANCIAL INSTRUMENTS

Fair value

The Company's recognized financial instruments consist of cash, accounts receivable, accounts payable, customer deposits and long-term debt. The values of cash, accounts receivable and accounts payable approximate their carrying amounts due to the short-term nature. As there is no secondary market for customer deposits, the calculation of a fair value with appropriate reliability is impractical.

It is not practical within the constraint of cost to determine the fair value of long-term liabilities with sufficient reliability.

Credit risk

The Company is exposed to credit risk from its customers. However, the Company has a large number of diverse customers minimizing concentration of credit risk.

CHATHAM-KENT HYDRO INC.
Notes to the Financial Statements
December 31, 2005

14. FUTURE INCOME TAXES

If the liability method of accounting for income taxes were used, a future tax asset of \$2,110,000, (2004 - \$2,715,000) would be recorded.

15. COMMITMENTS

The Company has entered into Service Level agreements with Chatham-Kent Utility Services Inc. to have them provide the services of billing, account collections, customer inquiries and meter reading as well as administrative services such as office space usage, rate submission support and accounting and budgeting support. The value for 2005 is \$2,870,981 (2004 - \$2,730,403).