

**HEARST POWER DISTRIBUTION COMPANY LIMITED/  
CORPORATION DE DISTRIBUTION  
ELECTRIQUE DE HEARST**

**AUDITORS' REPORT AND  
FINANCIAL STATEMENTS**

**DECEMBER 31, 2005**

## **AUDITORS' REPORT**

To the Shareholder of Hearst Power Distribution Company Limited/  
Corporation de distribution électrique de Hearst  
Hearst, Ontario

We have audited the balance sheet of the Hearst Power Distribution Company Limited/ Corporation de distribution électrique de Hearst as at December 31, 2005 and the statements of income, retained earnings and contributed capital and cash flow 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 corporation as at December 31, 2005 and the results of its operations for the year then ended in accordance with the accounting principles disclosed in the note 2 to the financial statements.

Chartered Accountants  
March 26, 2006  
MLM/lm

**HEARST POWER DISTRIBUTION COMPANY LIMITED/  
CORPORATION DE DISTRIBUTION  
ELECTRIQUE DE HEARST**

**FINANCIAL STATEMENTS**

**DECEMBER 31, 2005**

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**HEARST POWER DISTRIBUTION COMPANY LIMITED/  
CORPORATION DE DISTRIBUTION  
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**STATEMENT OF INCOME**

**YEAR ENDED DECEMBER 31, 2005**

	<b>Budget</b>	<b>2005 Actual</b>	<b>2004 Actual</b>
<b>SERVICE REVENUE</b>			
Electricity	\$ 6,023,287	\$ 6,962,269	\$ 6,009,684
Distribution	600,533	640,752	641,277
Wholesale market services, transmission and connection	1,911,617	1,851,650	1,799,017
	<u>8,535,437</u>	<u>9,454,671</u>	<u>8,449,978</u>
<b>COST OF SALES</b>			
Electricity	6,116,537	7,017,548	5,989,552
Wholesale market services	1,765,233	1,864,196	1,793,028
	<u>7,881,770</u>	<u>8,881,744</u>	<u>7,782,580</u>
<b>GROSS MARGIN</b>	653,667	572,927	667,398
<b>INTEREST INCOME</b>	84,000	102,393	93,868
<b>OTHER REVENUE</b>	39,992	55,324	73,132
	<u>777,659</u>	<u>730,644</u>	<u>834,398</u>
<b>EXPENDITURES DISTRIBUTION, OPERATION AND MAINTENANCE</b>			
Lines and feeders	185,540	205,966	208,155
Transformers	87,900	92,621	91,734
Meters	10,022	8,197	12,083
	<u>283,462</u>	<u>306,784</u>	<u>311,972</u>
<b>ADMINISTRATION AND FINANCE</b>			
Meter reading, billing and collecting	115,294	122,817	121,692
General administration	218,672	175,306	168,675
Interest on demand note	-		15,000
			<u>50,000</u>
	<u>333,966</u>	<u>313,123</u>	<u>340,367</u>
<b>AMORTIZATION</b>	138,603	108,950	131,059
<b>TOTAL EXPENDITURES</b>	<u>756,031</u>	<u>728,857</u>	<u>783,398</u>
<b>INCOME BEFORE PAYMENTS IN LIEU OF INCOME TAXES</b>			
	<u>21,628</u>	<u>1,787</u>	<u>51,000</u>
<b>PAYMENTS IN LIEU OF INCOME TAXES (RECOVERY)</b>			
Current	-		(453)
			10,025
Future	-		(22,800)
			<u>-</u>
	<u>21,628</u>	<u>(23,253)</u>	<u>10,025</u>
<b>NET INCOME</b>	<u>\$ 21,628</u>	<u>\$ 25,040</u>	<u>\$ 40,975</u>

**HEARST POWER DISTRIBUTION COMPANY LIMITED/  
CORPORATION DE DISTRIBUTION  
ELECTRIQUE DE HEARST**

**STATEMENT OF RETAINED EARNINGS  
AND CONTRIBUTED CAPITAL**

**YEAR ENDED DECEMBER 31, 2005**

	<u>2005</u>	<u>2004</u>
<b>RETAINED EARNINGS</b>		
BALANCE, BEGINNING OF YEAR	\$ 2,223,412	\$ 2,182,437
NET INCOME	<u>25,040</u>	<u>40,975</u>
BALANCE, END OF YEAR	\$ 2,248,452	\$ 2,223,412
<b>CONTRIBUTED CAPITAL</b>		
BALANCE, BEGINNING AND END OF YEAR	<u>\$ 553,783</u>	<u>\$ 553,783</u>

**HEARST POWER DISTRIBUTION COMPANY LIMITED/  
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**BALANCE SHEET**

**DECEMBER 31, 2005**

	<u>2005</u>	<u>2004</u>
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash	\$ 3,930,662	\$ 3,500,898
Unbilled revenue	1,233,530	1,016,825
Accounts receivable (note 3)	676,991	560,035
Income taxes recoverable	7,624	-
Inventory	102,177	112,925
Prepaid expenses	14,021	14,928
Future income taxes	22,800	-
	<u>5,987,805</u>	<u>5,205,611</u>
PRE-MARKET OPENING ENERGY VARIANCE	11,565	1,068
INVESTMENT (note 4)	32,585	33,256
PROPERTY AND EQUIPMENT (note 5)	1,050,562	1,090,723
OTHER ASSETS (note 6)	<u>18,095</u>	<u>19,368</u>
	<u>\$ 7,100,612</u>	<u>\$ 6,350,026</u>
<b>LIABILITIES</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable and accrued charges	\$ 2,436,475	\$ 1,656,294
Income taxes payable	-	8,025
Other regulatory liabilities	12,158	18,957
Due to Town of Hearst	96,054	133,227
Demand loan (note 8)	1,700,000	1,700,000
Customers deposits	<u>43,690</u>	<u>46,328</u>
	<u>4,288,377</u>	<u>3,562,831</u>
<b>SHAREHOLDER'S EQUITY</b>		
CAPITAL STOCK (note 9)	10,000	10,000
RETAINED EARNINGS	2,248,452	2,223,412
CONTRIBUTED CAPITAL	<u>553,783</u>	<u>553,783</u>
	<u>2,812,235</u>	<u>2,787,195</u>
	<u>\$ 7,100,612</u>	<u>\$ 6,350,026</u>

**HEARST POWER DISTRIBUTION COMPANY LIMITED/  
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**STATEMENT OF CASH FLOW**

**YEAR ENDED DECEMBER 31, 2005**

	<u>2005</u>	<u>2004</u>
<b>OPERATING ACTIVITIES</b>		
Net income	\$ 25,040	\$ 40,975
Items not requiring cash:		
Amortization	108,950	131,059
Future income taxes	(22,800)	-
	<u>111,190</u>	<u>172,034</u>
Changes in:		
Unbilled revenue	(216,705)	(106,642)
Accounts receivable	(116,956)	165,964
Income taxes recoverable/payable	(15,649)	39,525
Inventory	10,748	6,031
Prepaid expenses	907	(1,757)
Pre market opening energy variance	(10,497)	5,872
Accounts payable and accrued charges	780,181	189,634
Other regulatory liabilities	(6,799)	(5,872)
Due to Town of Hearst	(37,170)	17,478
Change in customers deposits	(2,638)	(11,049)
	<u>496,612</u>	<u>471,218</u>
<b>INVESTING ACTIVITIES</b>		
Purchase of property and equipment	(67,519)	(46,287)
Disposal (purchase) of investment	671	(9,255)
	<u>(66,848)</u>	<u>(55,542)</u>
<b>INCREASE IN CASH POSITION</b>	429,764	415,676
<b>CASH POSITION, BEGINNING OF YEAR</b>	<u>1,800,898</u>	<u>1,385,222</u>
<b>CASH POSITION, END OF YEAR (note 10)</b>	<u>\$ 2,230,662</u>	<u>\$ 1,800,898</u>

**HEARST POWER DISTRIBUTION COMPANY LIMITED/  
CORPORATION DE DISTRIBUTION  
ELECTRIQUE DE HEARST**

**NOTES TO FINANCIAL STATEMENTS**

**DECEMBER 31, 2005**

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**1. NATURE OF BUSINESS**

The corporation, incorporated under the Ontario Business Corporations Act, owns all the electrical distribution system in the territory of the Corporation of the Town of Hearst and is responsible for the distribution of the electrical power on this territory.

**RATE REGULATED ENTITY**

The Ontario Energy Board (OEB) has regulatory oversight of electricity matters in the Province of Ontario. Among other duties, the Board has the authority to issue distribution licences along with conditions pertaining to accounting records and filing requirements for rate setting purposes.

All energy has to be purchased through Independent Electricity System Operations (IESO) in a weighted average basis whereas the price paid for the electricity is based on the market price adjusted for the peak periods of demand.

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**2. SIGNIFICANT ACCOUNTING POLICIES**

The financial statements have been prepared in accordance with accounting principles for municipal electrical utilities in Ontario as required by statutes. Except for the principle of disposal of property and equipment and the principles explained under the heading regulation, all principles employed are in accordance with Canadian generally accepted accounting principles.

**REVENUE RECOGNITION**

Revenue from the sale of electricity is recorded on a basis of cyclical billings and also includes unbilled revenue accrued in respect of electricity delivered but not yet billed.

**INVENTORY**

Inventory is valued at the lower of cost and net realizable value. Most of the inventory is used for own purposes and is eventually added to the property and equipment. Cost is determined on the average cost basis.



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**NOTES TO FINANCIAL STATEMENTS**

**DECEMBER 31, 2005**

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**2. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)**

**PROPERTY AND EQUIPMENT**

Amortization of property and equipment is provided on a straight-line basis over the following periods:

Building and fixtures	50 years
Overhead lines and feeders	25 years
Underground lines and feeders	25 years
Transformers	25 years
Meters	25 years
Office equipment	10 years
Automotive equipment	5 years
Computer equipment	5 years
Other equipment	10 years

When property and equipment are disposed, the proceeds of disposition are recorded as a reduction to the appropriate property and equipment accounts. Consequently, gains and losses on disposals are brought into income over the depreciable lives of the remaining property and equipment.

**AMORTIZATION OF ORGANIZATION COSTS**

The organization costs are amortized on a straight line basis over 20 years.

**CUSTOMERS DEPOSITS**

Customers' advance deposits are cash collections from customers to mitigate the financial risk of non-payment of energy bills. Security deposits are refunded on customers account when a customer is deemed to have maintained a good payment history during the relevant time period set out in the customer security deposit policy.

**INCOME TAXES**

A municipal electric utility is exempt from tax under subsection 149 (1) of the Income Tax Act. Under the Electricity Act of 1998, municipal electric utilities have to make payments in lieu of taxes (PILS) to the province. These payments are generally equivalent to the income taxes that would be otherwise due if the municipal electric utility would have been taxable as a small business corporation under the Income Tax Act.

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**NOTES TO FINANCIAL STATEMENTS**

**DECEMBER 31, 2005**

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**2. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)**

**FUTURE INCOME TAXES**

Income taxes are provided, at current rates, for all items included in the statement of income regardless of the period in which such items are reported for income tax purposes. The principal item which results in timing differences between financial and tax reporting purposes is amortization. Future income taxes are adjusted for changes in income tax rates.

**EMPLOYEE FUTURE BENEFITS**

The company provides a pension plan for its employees through the Ontario Municipal Employees Retirement System (OMERS), a defined benefit plan established by the province. Both employers and employees are required to make contributions to the plan. The corporation's yearly contributions are expensed unless otherwise provided.

**INVESTMENT**

The investment in the buying group is recorded using the cost method. Yearly distributions from the investment are recorded as an increase in the assets and corresponding other income credit.

**REGULATION**

The entity has to follow regulatory accounting treatments that differ from Canadian generally accepted accounting policies for enterprises operating in non regulated environment.

Transition costs: certain costs to set up the company have been deferred in accordance with OEB guidelines. These costs have been increased for the prescribed OEB rate of return with an offsetting interest income credit.

Pre-market opening energy variance: this asset represents the utility's cost of power based on time-of-use rates and the amounts billed to non time-of-use customers. These costs have been increased for the prescribed OEB rate of return with an affecting interest income credit.

Other regulatory assets: OEB has allowed the deferral of their annual costs assessments. These costs will be subject to recovery starting in 2006 subject to OEB approval.

**HEARST POWER DISTRIBUTION COMPANY LIMITED/  
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**NOTES TO FINANCIAL STATEMENTS**

**DECEMBER 31, 2005**

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**2. SIGNIFICANT ACCOUNTING POLICIES (CONT'D)**

USE OF ESTIMATES

The presentation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reporting amount of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. These estimates are reviewed periodically, and, as adjustments become necessary, they are reported in the period in which they become known.

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**3. ACCOUNTS RECEIVABLE**

	<u>2005</u>	<u>2004</u>
Electrical energy	\$ 247,106	\$ 377,257
Qualifying transition costs	101,686	75,418
Other regulatory assets	207,766	1,989
Others	<u>123,126</u>	<u>108,225</u>
	679,684	562,889
Allowance for doubtful accounts	<u>2,693</u>	<u>2,854</u>
	<u>\$ 676,991</u>	<u>\$ 560,035</u>

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**4. INVESTMENT**

	<u>2005</u>	<u>2004</u>
Investment in Enerconnect Limited Partnership, a buying group for Municipal Electric Commissions		
Original cost	\$ 24,000	\$ 24,000
Share of limited partnership income	<u>8,585</u>	<u>9,256</u>
	<u>\$ 32,585</u>	<u>\$ 33,256</u>

The fair market value of the investment is not available.

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**NOTES TO FINANCIAL STATEMENTS**

**DECEMBER 31, 2005**

**5. PROPERTY AND EQUIPMENT**

	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>2005 Net</u>	<u>2004 Net</u>
Land	\$ 7,600	\$ -	\$ 7,600	\$ 7,600
Building and fixtures	201,570	63,820	137,750	141,512
Underground lines and feeders	1,979,561	1,363,640	615,921	627,949
Transformers	523,507	421,394	102,113	101,711
Meters	323,252	230,663	92,589	102,714
Office equipment	42,163	21,106	21,057	15,137
Automotive equipment	441,136	441,136	-	5,886
Computer equipment	133,281	107,366	25,915	42,222
Other equipment	123,917	78,713	45,204	43,156
Land rights	4,232	1,819	2,413	2,836
	<u>\$ 3,780,219</u>	<u>\$ 2,729,657</u>	<u>\$ 1,050,562</u>	<u>\$ 1,090,723</u>

**6. OTHER ASSETS**

	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>2005 Net</u>	<u>2004 Net</u>
Organisation costs	\$ 25,471	\$ 7,376	\$ 18,095	\$ 19,368

**7. BANK INDEBTEDNESS**

The corporation has an approved line of credit of 300,000\$, at prime, secured by a general security agreement on all of the company's assets.

**8. DEMAND LOAN**

	<u>2005</u>	<u>2004</u>
The Corporation of the Town of Hearst, promissory note, interest at the lesser of 12 % or a part of the net income for the year, payable on a monthly basis, no fixed capital repayment	\$ 1,700,000	\$ 1,700,000

**HEARST POWER DISTRIBUTION COMPANY LIMITED/  
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**NOTES TO FINANCIAL STATEMENTS**

**DECEMBER 31, 2005**

**9. CAPITAL STOCK**

	<u>2005</u>	<u>2004</u>
<b>AUTHORIZED</b>		
Unlimited number of preference shares, dividends at the discretion of the directors, non voting		
Unlimited number of common shares		
<b>ISSUED</b>		
10,000 common shares	\$ 10,000	\$ 10,000

**10. STATEMENT OF CASH FLOW**

**CASH POSITION**

Cash position consists of cash on hand, balances with banks and the demand loan with the Town of Hearst and is comprised of the following balance sheet amounts:

	<u>2005</u>	<u>2004</u>
Cash	\$ 3,930,662	\$ 3,500,898
Demand loan	(1,700,000)	(1,700,000)
	<u>\$ 2,230,662</u>	<u>\$ 1,800,898</u>

**INTEREST AND INCOME TAXES**

Cash payments were made for the following items:

	<u>2005</u>	<u>2004</u>
Interest	\$ 60,531	\$ 5,757
Income taxes	18,025	2,000
	<u>\$ 78,556</u>	<u>\$ 7,757</u>

**HEARST POWER DISTRIBUTION COMPANY LIMITED/  
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**NOTES TO FINANCIAL STATEMENTS**

**DECEMBER 31, 2005**

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**11. RELATED PARTY TRANSACTIONS**

During the year, the company incurred the following related party transactions with its sole shareholder, the Corporation of the Town of Hearst.

	<u>2005</u>	<u>2004</u>
Service revenue	\$ 470,208	\$ 456,077
Rent expense	8,164	8,012
Clerical and answering services expense	24,002	23,259
Interest on demand loan	-	50,000

These transactions are in the normal courses of operations and are measured at the exchange amount which is received and paid on similar terms as those of unrelated parties.

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**12. FINANCIAL INSTRUMENTS**

The company's financial instruments consists of cash, accounts receivable, temporary and long-term investments, demand loan, accounts payable and accrued changes, amounts due to related parties. Unless otherwise noted, it is management's opinion that the company is not exposed to significant interest, currency or credit risks arising from these financial instruments. The fair values of these financial instruments approximated their carrying values, unless otherwise noted.

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