

Consolidated Financial Statements of

EPCOR UTILITIES INC.

Years ended December 31, 2010 and 2009

Management's responsibility for financial reporting

The preparation and presentation of the accompanying consolidated financial statements of EPCOR Utilities Inc. are the responsibility of management and the consolidated financial statements have been approved by the Board of Directors. In management's opinion, the consolidated financial statements have been prepared within reasonable limits of materiality in accordance with Canadian generally accepted accounting principles. The preparation of financial statements necessarily requires judgment and estimation when events affecting the current year depend on determinations to be made in the future. Management has exercised careful judgment where estimates were required, and these consolidated financial statements reflect all information available to March 11, 2011. Financial information presented elsewhere in this annual report is consistent with that in the consolidated financial statements.

To discharge its responsibility for financial reporting, management maintains systems of internal controls designed to provide reasonable assurance that the Company's assets are safeguarded, that transactions are properly authorized and that reliable financial information is relevant, accurate and available on a timely basis. The internal control systems are monitored by management, and evaluated by an internal audit function that regularly reports its findings to management and the Audit Committee of the Board of Directors.

The consolidated financial statements have been examined by KPMG LLP, the Company's external auditors. The external auditors are responsible for examining the consolidated financial statements and expressing their opinion on the fairness of the financial statements in accordance with Canadian generally accepted accounting principles. The auditors' report outlines the scope of their audit examination and states their opinion.

The Board of Directors, through the Audit Committee, is responsible for ensuring management fulfils its responsibilities for financial reporting and internal controls. The Audit Committee, which is comprised of independent directors, meets regularly with management, the internal auditors and the external auditors to satisfy itself that each group is discharging its responsibilities with respect to internal controls and financial reporting. The Audit Committee reviews the consolidated financial statements and management's discussion and analysis and recommends their approval to the Board of Directors. The external auditors have full and open access to the Audit Committee, with and without the presence of management. The Audit Committee is also responsible for reviewing and recommending the annual appointment of the external auditors and approving the annual external audit plan.

On behalf of management,



Don Lowry
President and Chief Executive Officer



Mark Wiltzen
Senior Vice President and
Chief Financial Officer

March 11, 2011

EPCOR UTILITIES INC.

Consolidated Financial Statements

Years ended December 31, 2010 and 2009

Auditors' Report	1
Financial Statements:	
Consolidated Statements of Income	2
Consolidated Balance Sheets	3
Consolidated Statements of Changes in Shareholder's Equity	5
Consolidated Statements of Comprehensive Income	6
Consolidated Statements of Cash Flows	7
Notes to Consolidated Financial Statements	8



KPMG LLP
Chartered Accountants
10125 – 102 Street
Edmonton AB T5J 3V8
Canada

Telephone (780) 429-7300
Fax (780) 429-7379
Internet www.kpmg.ca

INDEPENDENT AUDITORS' REPORT

To the Shareholder

We have audited the accompanying consolidated financial statements of EPCOR Utilities Inc. which comprise the consolidated balance sheets as at December 31, 2010 and 2009, the consolidated statements of income, comprehensive income, changes in shareholder's equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of EPCOR Utilities Inc. as at December 31, 2010 and 2009, and the results of its consolidated operations and its consolidated cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Chartered Accountants

March 11, 2011
Edmonton, Canada

EPCOR UTILITIES INC.

Consolidated Statements of Income
(In millions of dollars)

Years ended December 31, 2010 and 2009

	2010	2009
Revenues	\$ 1,473	\$ 2,354
Expenses (income):		
Energy purchases and fuel	746	1,256
Operations, maintenance and administration	366	513
Franchise fee, property taxes and other taxes	61	74
Depreciation, amortization and asset retirement accretion (note 6)	88	179
Foreign exchange losses	-	2
Equity share of income of Capital Power and other (note 3)	(88)	(65)
Loss on sale of a portion of investment in Capital Power (note 3)	33	-
Net financing expenses (note 18)	127	159
Gain on sale of power syndicate agreement (note 5c)	-	(30)
Loss on sale of power generation business (note 4)	-	92
	1,333	2,180
Income before income taxes and non-controlling interests	140	174
Income taxes (note 19)	7	27
Income before non-controlling interests	133	147
Non-controlling interests (note 14)	-	22
Net income	\$ 133	\$ 125

See accompanying notes to consolidated financial statements.

EPCOR UTILITIES INC.

Consolidated Balance Sheets
(In millions of dollars)

December 31, 2010 and 2009

	2010	2009
Assets		
Current assets:		
Cash and cash equivalents (note 27)	\$ 104	\$ 11
Accounts receivable	279	243
Income taxes recoverable	-	2
Inventories	10	11
Prepaid expenses	3	2
Future income tax assets (note 19)	1	1
Current portion of long-term receivables (note 8)	237	255
	<hr/> 634	<hr/> 525
Property, plant and equipment (note 6)	1,907	1,778
Contract and customer rights and other intangible assets (note 7)	100	110
Future income tax assets (note 19)	41	40
Long-term receivables (note 8)	419	643
Investment in Capital Power (note 3)	1,235	1,481
Other assets (note 9)	178	164
	<hr/> \$ 4,514	<hr/> \$ 4,741

Approved on behalf of the Board:



Hugh J. Bolton
Director and Chair of the Board



Alexander M. Davidson
Director and Chair of the Audit Committee

	2010	2009
Liabilities and Shareholder's Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 273	\$ 241
Income taxes payable	6	-
Other current liabilities	36	32
Current portion of long-term debt (note 11)	219	225
	534	498
Long-term debt (note 11)	1,456	1,692
Other non-current liabilities (note 12)	58	81
Future income tax liabilities (note 19)	1	-
	2,049	2,271
Shareholder's equity:		
Share capital and contributed surplus (notes 5b, 15 and 24)	24	24
Retained earnings	2,459	2,462
Accumulated other comprehensive loss (note 16)	(18)	(16)
	2,465	2,470
Contingencies and commitments (note 26)		
Subsequent events (note 29)		
	\$ 4,514	\$ 4,741

See accompanying notes to consolidated financial statements.

EPCOR UTILITIES INC.

Consolidated Statements of Changes in Shareholder's Equity
(In millions of dollars)

Years ended December 31, 2010 and 2009

	2010	2009
Share capital and contributed surplus:		
Balance, beginning of year	\$ 24	\$ -
Capital contribution (note 5b)	-	24
Balance, end of year	24	24
Retained earnings:		
Balance, beginning of year	2,462	2,476
Adjustment for changes in accounting policies	-	1
Net income	133	125
Common share dividends paid	(136)	(134)
Refundable taxes (note 19)	-	(6)
Balance, end of year	2,459	2,462
Accumulated other comprehensive loss:		
Balance, beginning of year	(16)	(47)
Other comprehensive (loss) income	(2)	31
Balance, end of year (note 16)	(18)	(16)
Total shareholder's equity, end of year	\$ 2,465	\$ 2,470

See accompanying notes to consolidated financial statements.

EPCOR UTILITIES INC.

Consolidated Statements of Comprehensive Income
(In millions of dollars)

Years ended December 31, 2010 and 2009

	2010	2009
Net income	\$ 133	\$ 125
Other comprehensive (loss) income, net of income taxes:		
Equity in other comprehensive (loss) income from Capital Power (note 3) ¹	(4)	16
Unrealized losses on derivative instruments designated as cash flow hedges ²	-	(1)
Reclassification of losses on derivative instruments designated as cash flow hedges to net income ³	-	12
Unrealized loss in self-sustaining foreign operations ⁴	-	(25)
Non-controlling interests ⁴	-	17
Losses realized in net income upon sale of power generation business ⁵	-	12
Losses realized in net income upon sale of a portion of investment in Capital Power ⁶ (note 3)	2	-
	(2)	31
Comprehensive income	\$ 131	\$ 156

¹ For the years ended December 31, 2010 and 2009, net of income tax recoveries of \$1 and income tax expense of \$2 respectively.

² For the year ended December 31, 2009, net of income tax expense of nil.

³ For the year ended December 31, 2009, net of reclassification of income tax recoveries of \$5.

⁴ For the year ended December 31, 2009, net of income tax expense of nil.

⁵ For the year ended December 31, 2009, net of reclassification of income tax recoveries of \$2.

⁶ For the year ended December 31, 2010, net of reclassification of income tax recoveries of nil.

See accompanying notes to consolidated financial statements.

EPCOR UTILITIES INC.

Consolidated Statements of Cash Flows
(In millions of dollars)

Years ended December 31, 2010 and 2009

	2010	2009
Operating activities:		
Net income	\$ 133	\$ 125
Adjustments to reconcile net income to cash flows from operating activities:		
Depreciation, amortization and asset retirement accretion (note 6)	88	179
Gain on sale of power syndicate agreement (note 5c)	-	(30)
Non-controlling interests in Capital Power Income L.P. (note 14)	-	19
Loss on sale of power generation business (note 4)	-	92
Loss on sale of a portion of investment in Capital Power (note 3)	33	-
Equity share of income of Capital Power and other (note 3)	(88)	(65)
Fair value changes on derivative instruments	-	(23)
Unrealized foreign exchange gains	-	(3)
Fair value (gains) losses on floating-rate notes	(5)	5
Future income taxes	(1)	40
Other	(4)	17
	156	356
Change in non-cash operating working capital (note 17)	9	(54)
	165	302
Investing activities:		
Property, plant and equipment and other assets	(218)	(517)
Change in non-cash investing working capital (note 17)	(4)	(27)
Proceeds on sale of Castleton	-	12
Proceeds on sale of power syndicate agreement (note 5c)	-	47
Payment of Gold Bar transfer fee (note 5b)	(15)	(17)
Proceeds on sale of power generation business (note 4)	-	468
Proceeds on sale of a portion of investment in Capital Power (note 3)	212	-
Distributions from Capital Power (note 3)	87	18
Payment received on long-term receivables	245	39
Other	(2)	4
	305	27
Financing activities:		
Net repayment of short-term debt	-	(211)
Proceeds from issuance of long-term debt	-	238
Repayment of long-term debt	(241)	(276)
Distributions to non-controlling interests	-	(47)
Common share dividends paid	(136)	(134)
Debt issue costs and other	-	(2)
	(377)	(432)
Foreign exchange gain on cash held in a foreign currency	-	3
Increase (decrease) in cash and cash equivalents	93	(100)
Cash and cash equivalents, beginning of year	11	111
Cash and cash equivalents, end of year	\$ 104	\$ 11
Supplementary cash flow information:		
Interest paid net of interest received	\$ 133	\$ 148
Income taxes paid net of income taxes recovered	-	18

See accompanying notes to consolidated financial statements.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

1. Description of business:

(a) Nature of operations:

EPCOR Utilities Inc. (the Company or EPCOR) builds, owns and operates electrical transmission and distribution networks, water and wastewater treatment facilities and infrastructure, and provides electricity and water services and products to residential and commercial customers. The Company operates in Canada with its head office located in Edmonton, Alberta.

The common shares of EPCOR are owned by The City of Edmonton (the City). The Company was established by Edmonton City Council (City Council) under City Bylaw 11071.

(b) Rate regulation:

EPCOR provides rate-regulated electric distribution and transmission services to customers within Edmonton and surrounding areas, and supplies electricity under Regulated Rate Tariffs (RRT) to customers in Alberta. EPCOR's electric distribution and transmission operations and its RRT operations are regulated by the Alberta Utilities Commission (AUC), pursuant to the *Electric Utilities Act* (Alberta), the *Public Utilities Board Act* (Alberta) and the *Hydro and Electric Energy Act* (Alberta). The AUC administers these acts and regulations regarding tariffs, rates, construction, financing, operations, accounting and service area. The distribution and transmission and RRT businesses operate under cost-of-service regulation, whereby the AUC issues rate orders establishing the revenue requirements of these businesses, which are those revenues required to recover approved operating costs and to provide a rate of return on a deemed capital structure applied to approved rate base assets. The approved 2010 return on equity (ROE) for the distribution and transmission business was 9.00% (2009 – 9.00%).

The RRT business is required to file rate applications with the AUC for the approval of RRT energy and non-energy billing rates. After a process of public consultation is completed, the AUC approves the rates for the specified period. Energy rates under an Energy Price Setting Plan (EPSP), which determines the energy margin, the procurement methodology and energy billing rates for the Company's RRT customers, were approved by the AUC in 2006 for the period ending June 30, 2011. During the year, the AUC approved the Company's request to enter into a negotiation process with consumer interest groups with respect to its EPSP for the period July 1, 2011 to December 31, 2012 and potentially extending to June 30, 2014. The Company expects to reach a settlement and obtain approval from the AUC in the second quarter of 2011. The Company applies for non-energy rates based on estimated costs of service. Once the rates are approved, they are not adjusted as a result of actual costs of service being different from those which were estimated other than for certain prescribed costs that are eligible for deferral account treatment. Such rates include a 6.00% return margin on non-energy costs and a 6.00% return on the prescribed equity portion of the rate base, pursuant to a negotiated settlement application submitted in August 2010.

The AUC approved 2010 and 2011 non-energy billing rates for the RRT business in December 2010, and 2010 and 2011 rates for the distribution and transmission business in November 2010, except for allocated corporate costs. The AUC concluded that it was not in a position to determine the proper regulatory treatment for allocated corporate costs following the sale of the power generation business to Capital Power. The AUC directed that a separate module for this proceeding be convened in order to further review allocated corporate costs. The Company filed its submission of the separate module in late December 2010. On March 1, 2011, the Company and intervenors (representing customers) to the 2010 - 2011 General Tariff Applications reached a negotiated settlement in principle regarding EPCOR's allocated corporate costs. EPCOR and the intervenors have jointly applied to the AUC for approval of the negotiated settlement and if approved, the separate module for the review of allocated corporate costs will be concluded. After reviewing the proposed settlement or

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

completion of the separate module, it is expected that the AUC will make a final determination on the matter of allocated corporate costs in the first half 2011 and the final determination will then be reflected in non-energy rates and distribution and transmission rates.

EPCOR's water treatment and distribution services to customers within the City are rate regulated by City Council pursuant to a performance-based rates (PBR) bylaw. The City is the Company's common shareholder and is therefore a related party. Rates approved pursuant to this bylaw are intended to allow the Company to recover its operating costs and earn a ROE of 11.25% (2009 – 11.25%), while also providing an incentive to manage costs below inflation. If performance targets outlined in the PBR bylaw are achieved, water rates are increased by the annual change in the rate of inflation less an efficiency factor of 25 basis points.

The current PBR bylaw has been approved by City Council for a five-year period through to March 31, 2012.

Water sales to regional water commissions that supply water to communities surrounding Edmonton are rate regulated by the AUC on a complaints-only basis, whereby such communities may apply to the AUC to resolve disputes in connection with EPCOR's rates, tolls or charges. EPCOR sets the rates charged to the regional water commissions to recover related operating and capital costs plus a ROE.

Wastewater treatment services provided at EPCOR's Gold Bar Wastewater Treatment Plant (Gold Bar) are rate-regulated by City Council. The Master Agreement for the transfer of Gold Bar to EPCOR contains provisions to address ongoing operations and to allocate the City Council-approved sanitary utility fees charged to City residents and businesses to both EPCOR for wastewater treatment and the City of Edmonton's Drainage Services department (Drainage Services) for collection and transmission of wastewater to Gold Bar. EPCOR's return on equity and net income are influenced by the revenue allocation between EPCOR and Drainage Services, which is based on a relative cost of service basis between the collection and transmission and wastewater treatment functions, and the ability to obtain approval for sanitary utility rate increases from its regulator, City Council, that provide for the recovery of expenditures and the earning of a fair ROE.

2. Summary of significant accounting policies:

(a) Basis of presentation:

These consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles (GAAP).

These consolidated financial statements include the accounts of EPCOR, its subsidiaries, and its proportionate share of assets, liabilities, revenues and expenses of joint ventures. Prior to the sale of the power generation business in July 2009, the consolidated financial statements included the accounts of the Company's approximate 31% interest in Capital Power Income L.P. (CPILP) (formerly EPCOR Power L.P.). Under GAAP, EPCOR controlled CPILP which therefore was a subsidiary of EPCOR. In these consolidated financial statements, Capital Power refers to Capital Power Corporation and its directly and indirectly owned subsidiaries including Capital Power L.P., except where otherwise noted or the context otherwise indicates. Subsequent to the sale of the power generation business (note 4) and the sale of a portion of EPCOR's investment in Capital Power (note 3), EPCOR has an approximate 61% interest in the power generation business through its equity investment in Capital Power. Under GAAP, EPCOR has significant influence, but not control of Capital Power and therefore has used the equity method to account for its investment in Capital Power.

All significant intercompany balances and transactions have been eliminated on consolidation.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

(b) Changes in significant accounting policies:

Future accounting changes

The CICA has mandated that Canadian reporting issuers, like EPCOR, will need to begin reporting under International Financial Reporting Standards (IFRS), including comparative figures, by the first quarter of 2011. The Company is currently finalizing its IFRS conversion project which includes assessing the impact of the differences in accounting standards on the Company's future financial reporting requirements.

(c) Regulatory accounting:

The Company accounts for certain transactions in accordance with applicable rate regulation (regulatory accounting). As permitted under GAAP, the Company applies standards issued by the Financial Accounting Standards Board (FASB) in the United States as another source of GAAP. FASB Accounting Standards Codification Section 980 - Regulated Operations, represents the standards the Company applies for regulatory accounting. Under regulatory accounting, the timing of the Company's recognition of certain assets, liabilities, revenues and expenses may differ from that otherwise expected under Canadian GAAP for non-rate-regulated enterprises.

Certain separate assets and liabilities have been recognized solely as a result of the effects of rate regulation. At December 31, 2010 and 2009, these assets and liabilities are not material and for the years then ended the income statement impact is not material.

For the Company's rate-regulated enterprises, the following accounting principles apply:

- (i) *Asset disposals and retirements* - For rate-regulated transmission, distribution and RRT businesses, when an asset other than land or buildings is retired or disposed of, any proceeds are recorded as a reduction to the cost of the replacement asset, no gain or loss is reflected in income, and the related cost and accumulated depreciation are not removed until the end of the originally estimated useful life. Where there is no replacement asset, the proceeds are recorded as a reduction of the next most similar asset capitalized. On disposals of land and buildings, any difference between the proceeds and cost are recognized in income, the cost and accumulated depreciation are removed, and the accumulated depreciation on buildings is recorded in a deferral account to be returned to the rate payer in a future tariff application.

For rate-regulated water services businesses, any proceeds or salvage value is recorded in accumulated depreciation, with no gain or loss reflected in income at the time of retirement or disposition. The results of the disposal or retirement are then recognized in future depreciation rates and depreciation charges. Cost and accumulated depreciation balances of retired assets are removed. In the case where an entire asset class ceases to exist, net proceeds in excess of accumulated depreciation are recorded as a gain on sale.

Non-rate-regulated entities include gains or losses on disposal of property, plant and equipment in net income at the time of retirement or disposition and the original cost and accumulated depreciation are removed.

- (ii) *Asset removal costs* - For rate-regulated transmission, distribution and RRT businesses, costs to remove an asset are included in the cost of the replacement asset. For rate-regulated water services businesses, future costs for decommissioning of assets are provided for based on estimated removal and site restoration costs, net of salvage value, as approved by the regulator. These amounts are recorded as a provision for plant decommissioning on the balance sheet with a corresponding increase in the cost of the related asset. Upon the retirement of water utility assets, the removal and site restoration costs, net of salvage value, are charged to the provision for plant decommissioning. The removal and site restoration costs for these assets are based on

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

independent studies of plant decommissioning and site restoration commissioned by the Company and, where applicable, as directed by the regulator. Asset retirement obligations for non-regulated entities are recognized in the period in which they are incurred as described in note 2(o).

- (iii) *Allowance for funds used during construction (AFUDC)* - The Company capitalizes AFUDC to provide for the cost of capital invested in rate-regulated construction activities. AFUDC is applied during construction at the weighted average cost of capital of the particular rate-regulated operations, as approved by the regulator.
 - (iv) *Intercompany profit on sales to rate-regulated affiliates* - The Company does not eliminate intercompany profits arising from sales within the consolidated group of EPCOR companies and included in assets remaining within its rate-regulated businesses, as the intercompany profit is deemed to have been realized to the extent that the sales price is recognized for rate-making purposes by the regulator. Intercompany profits included in assets remaining with a non-rate-regulated entity within the consolidated group are unrealized and are eliminated upon consolidation.
- (d) Measurement uncertainty:

The preparation of the Company's financial statements, in accordance with Canadian GAAP, requires management to make estimates that affect the reported amounts of revenues, expenses, assets and liabilities as well as the disclosure of contingent assets and liabilities at the financial statement date.

By regulation, wire service providers in Alberta are not required to submit final load settlement data on customer electricity usage until eight months after the month in which such electricity was consumed. The data and associated processes and systems used by the Company to estimate electricity revenues and costs, including unbilled consumption, are complex. The Company's estimation procedures will not necessarily detect errors in underlying data provided by industry participants including wire service providers and load settlement agents.

The amount of revenues and related profit recognized under the percentage of completion method for certain plant construction and other project upgrades described in note 2(e) depends on accuracy of cost, schedule and performance estimates and estimates related to the ability to recover additional contract costs through change orders or claims to the customer or contractors.

For certain accounting measures such as determining asset impairments, recording financial assets and liabilities, recording certain non-financial derivatives and for certain disclosures, the Company is required to estimate the fair value of certain assets or obligations. Estimates of fair value may be based on readily determinable market values or on depreciable replacement cost or discounted cash flow techniques employing estimated future cash flows based on a number of assumptions and using an appropriate discount rate.

Measurement of certain of the Company's pension costs and plan assets and obligations requires the use of estimates with respect to expected plan investment performance, salary escalation, retirement ages of employees, timing of related future cash flows and appropriate discount rates for use in discounted cash flow and actuarial techniques.

Depreciation and amortization is an estimate to allocate the cost of an asset over its estimated useful life on a systematic and rational basis. Estimating the appropriate useful lives of assets requires significant judgment and is generally based on estimates of common life characteristics of common assets.

Income taxes are determined based upon estimates of the Company's current income taxes and estimates of future income taxes resulting from temporary tax differences. Future income tax assets are assessed to determine the likelihood that they will be realized from future taxable income. To the

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

extent that realization is not considered likely, a valuation allowance is recorded and charged against income in the period that the allowance is created or revised.

Certain estimates are necessary since the regulatory environment that the Company operates in often requires amounts to be recorded at estimated values until finalization and adjustment pursuant to subsequent regulatory decisions, or other regulatory proceedings.

Adjustments to previous estimates, which may be material, will be recorded in the period they become known.

(e) Revenue recognition:

Revenues from the sales of electricity and water are recognized upon delivery. These revenues include an estimate of the value of electricity and water consumed by customers, but billed subsequent to year-end.

Revenues from the sale of goods are recognized when the products have been delivered. Revenues from services are recognized when the service has been performed or delivered.

Certain Water Services contracts constitute multiple-deliverable arrangements. Certain deliverables of these arrangements are separately accounted for, provided the delivered elements have stand-alone value to the customer, the fair value of any undelivered elements can be objectively and reliably determined and there is no general right of return. These identifiable deliverables may include, but are not limited to, plant construction and project upgrades and expansions, financing or leasing of upgrades and facilities operations. For arrangements which include multiple deliverables and for which the criteria for recognition as a multiple-deliverable arrangement are met, the total contract value is allocated to each element based on its relative fair value and the Company's relevant revenue recognition policies are applied to each element. When the stated contract consideration associated with an undelivered item is contingent upon delivery, revenue related to each deliverable with contingent revenues is recognized based on the lesser of the relative fair value and the non-contingent revenues.

Finance income earned from arrangements accounted for as direct financing leases is accounted for as described in note 2(p).

Revenue from plant construction and other project upgrades and expansions provided to customers is recognized on the percentage of completion basis. Percentage of completion is estimated based on an assessment of progress towards the completion of contract tasks or milestones. These estimates result in the recognition of unbilled receivables, which are reported net of billings to customers for the construction work. Provisions for estimated losses on uncompleted contracts are made for the full amount of the projected loss in the period in which the losses are identified. Revenues and costs related to change orders are included in total estimated contract revenue and expenses when approval is reasonably assured. Revenue from the financing of the upgrades and expansions is recognized over the term of each contract using the effective interest method based on the fair value of the loan calculated at the inception of each contract.

(f) Financial instruments:

Financial assets are identified and classified as either available for sale, held for trading, held to maturity, or loans and receivables. Financial liabilities are classified as either held for trading or other liabilities. Initially, all financial assets and financial liabilities are recorded on the balance sheet at fair value with subsequent measurement determined by the classification of each financial asset and liability.

Financial assets and financial liabilities held for trading are measured at fair value with the changes in fair value reported in net income. Financial assets held to maturity, loans and receivables and financial

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

liabilities other than those held for trading are measured at amortized cost. Available-for-sale financial assets are measured at fair value with changes in fair value reported in other comprehensive income until the financial asset is disposed of or becomes impaired. Investments in equity instruments classified as available for sale that do not have quoted market prices in an active market are measured at cost.

Upon initial recognition, the Company may designate financial instruments as held for trading when such financial instruments have a reliably determinable fair value and where doing so eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets and liabilities or recognizing gains and losses on them on a different basis. The Company has designated its cash and cash equivalents and investment in floating-rate notes as held for trading. All other non-derivative financial assets not meeting the Company's criteria for designating as held for trading are classified as available for sale, loans and receivables or held to maturity.

Financial assets purchased or sold, where the contract requires the asset to be delivered within an established timeframe, are recognized on a settlement date basis.

Transaction costs on financial assets and liabilities classified as other than held for trading are capitalized and amortized over the expected life of the instrument, based on contractual cash flows, utilizing the effective interest method. The effective interest method calculates the amortized cost of a financial asset or liability and allocates the interest income or expense over the term of the financial asset or liability using an effective interest rate.

(g) Income taxes:

Under the *Income Tax Act* (Canada) (ITA), a municipally owned corporation is subject to income tax on its taxable income if the income from activities for any relevant period that was earned outside the geographical boundaries of the municipality exceeds 10% of the corporation's total income for that period. As a result of these and other provisions, certain Canadian subsidiaries of the Company are taxable under the ITA and provincial income tax acts. The Company's U.S. subsidiaries are subject to income tax pursuant to U.S. federal and state tax laws.

The Company follows the asset and liability method of accounting for income taxes. Under this method, current income taxes are recognized for the estimated income taxes payable or recoverable for the current year. Future income tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future income tax assets and liabilities are measured using enacted or substantively enacted rates of tax expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on future tax assets and liabilities is recognized in income in the period that includes the date of enactment or substantive enactment.

(h) Cash and cash equivalents:

Cash and cash equivalents include cash or highly liquid, investment-grade, short-term investments and are recorded at fair market value.

(i) Inventories:

Small parts and other consumables, the majority of which are consumed by the Company in the provision of its goods and services, are valued at the lower of cost and net realizable value. Cost includes the purchase price, transportation costs and other costs to bring the inventories to their present location and condition. The cost of any assembled inventory includes direct labor, materials and attributable overhead. The costs of inventory items that are interchangeable are determined on an average cost basis. For inventory items that are not interchangeable, cost is assigned using specific

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

identification of their individual costs. Previous write downs of inventories from cost to net realizable value can be fully or partially reversed if supported by economic circumstances.

(j) Investments:

Investments in which the Company exercises significant influence are accounted for using the equity method. Other investments are classified as available for sale and are recorded at fair value unless the investments do not have a quoted market price in an active market in which case the investments are recorded at cost. Investments recorded at cost for which there is a decline in fair value below cost that is other than temporary are written down and the loss is recognized in net income.

(k) Property, plant and equipment:

Property, plant and equipment are recorded at cost and include contracted services, materials, interest, direct and indirect labor, overhead costs, asset retirement costs, and net revenues during the pre-operating period. Certain assets may be acquired or constructed with financial assistance in the form of contributions from developers or customers and non-repayable government grants. Contributions received for financing the costs of assets are recorded as a reduction of the related asset cost.

Depreciation on property, plant and equipment is provided on the straight-line basis over their estimated useful lives. The regulator approves depreciation rates for rate-regulated assets. No depreciation is provided on construction work in progress.

The Company capitalizes interest during construction for non-rate-regulated operations to provide for the costs of borrowing on construction activities. Interest is applied during construction using the average cost of debt associated with the specific project. The Company's rate-regulated operations capitalize AFUDC.

Repairs and maintenance expenditures are capitalized if they extend the life of an existing asset, enhance the service potential of an existing asset, or result in a tangible asset with a useful life in excess of one year. In non rate-regulated business units, items meeting the capitalization criteria are capitalized only if the cost exceeds an established threshold. For rate-regulated operations, there is no threshold since an asset is capitalized if it has been approved by the regulator.

(l) Contract and customer rights and other intangible assets:

Customer rights represent the costs to acquire the rights to provide electricity services to particular customer groups. The costs are amortized on a straight-line basis over twenty years depending on the expectation of benefit from the underlying customer group.

Software intangibles are amortized on a straight-line basis over terms ranging from one to twenty years.

(m) Other assets:

The floating-rate notes (note 9) that were received in exchange for non-bank sponsored asset backed commercial paper are recorded at fair value and are classified as a non-current asset due to the expected maturity dates of the notes.

Loans and other long-term receivables, which are classified as loans and receivables and measured at amortized cost, are comprised of promissory notes receivable and amounts due from customers more than one year from the balance sheet date and will be repaid between 2012 and 2029 (note 8).

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

(n) Impairment of long-lived assets:

The Company reviews the valuation of long-lived assets subject to depreciation and amortization when events or changes in circumstances may indicate or cause a long-lived asset's carrying amount to exceed the total undiscounted future cash flows expected from its use and eventual disposition. An impairment loss, if any, would be recorded as the excess of the carrying amount of the asset over its fair value, measured by either market value, if available, or estimated by calculating the present value of expected future cash flows related to the asset.

(o) Asset retirement obligations:

The Company recognizes asset retirement obligations in the period in which they are incurred, unless the fair value cannot be reasonably determined. A corresponding asset retirement cost is added to the carrying amount of the associated long-lived asset, and is depreciated over the estimated useful life of the asset. Accretion of the liability due to the passage of time is an operating expense, and is recorded over the estimated time period until settlement of the obligation.

The Company is legally required to remove its rate-regulated distribution, transmission and water long-lived assets at the end of their useful lives and restore to original condition their associated sites. However, as the lives of these assets are indeterminate, the Company has not recorded asset retirement obligations since the estimated fair value of the obligations are not reasonably determinable. While the asset retirement obligations cannot be reasonably determined, the Company records a provision for decommissioning on its rate-regulated water assets as approved by its regulator.

(p) Leases or arrangements containing a lease:

Leases or other arrangements entered into for use of property, plant and equipment are classified as either capital or operating leases. Leases or other arrangements that transfer substantially all of the benefits and risks of ownership of property to the Company are classified as capital leases. Equipment acquired under capital leases is depreciated over the term of the lease. Rental payments under operating leases are expensed as incurred.

Finance income related to leases or arrangements accounted for as either direct financing leases or as sales-type leases is recognized in a manner that produces a constant rate of return on the net investment in the lease. The net investment in both direct financing leases and sales-type leases is composed of net minimum lease payments and unearned finance income. Unearned finance income on direct financing leases is the difference between the total minimum lease payments and the carrying amount of the leased property. Unearned finance income on sales-type leases is the difference between the total minimum lease payments and the aggregate present values of the minimum lease payments. Unearned finance income for both direct financing leases and sales-type leases is deferred and recognized in net income over the lease term.

(q) Employee future benefits:

The employees of the Company are either members of the Local Authorities Pension Plan (LAPP) or other defined contribution or defined benefit plans.

The LAPP is a multiemployer defined benefit pension plan. The Trustee of the plan is the Treasurer of Alberta and the plan is administered by a Board of Trustees. The Company and its employees make contributions to the plan at rates prescribed by the Board of Trustees to cover costs under the plan. Since the plan is a multiemployer plan, it is accounted for as a defined contribution plan. Accordingly, the Company does not recognize its share of any plan surplus or deficit.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

The Company maintains additional defined contribution and defined benefit pension plans to provide pension benefits to those employees (comprising less than 1% (2009 – 10%) of total employees) who are not otherwise served by LAPP, including employees of new or acquired operations.

The Company accrues its obligations for its defined benefit pension plans net of plan assets. The cost of pension benefits earned by employees is actuarially determined using the projected benefit method pro-rated on services and management's best estimate of expected plan investment performance, salary escalation and retirement ages of employees. For the purpose of calculating the expected return on plan assets, those assets are valued at quoted market value. The discount rate used to calculate the interest cost on the accrued benefit obligation is determined by reference to market interest rates at the balance sheet date on high-quality debt instruments with cash flows that match the timing and amount of expected benefit payments. Past service costs from plan amendments are amortized on a straight-line basis over the estimated average remaining service of employees active at the date of amendment. The excess of the net cumulative unamortized actuarial gain or loss over 10% of the greater of the accrued benefit obligation and the market value of plan assets is amortized over the estimated average remaining service period of the active employees.

(r) Offsetting of financial assets and financial liabilities:

Financial assets and financial liabilities are presented on a net basis when the Company has a legally enforceable right to set-off the recognized amounts and intends to settle on a net basis or to realize the asset and settle the liability simultaneously.

(s) Long-term debt discounts, premiums and issue expenses:

Debenture discounts, premiums and issue expenses with respect to long-term debt are amortized over the term of the related debt using the effective interest rate method.

3. Investment in Capital Power

EPCOR holds 47.4 million exchangeable limited partnership (L.P.) units of Capital Power L.P. (exchangeable for common shares of Capital Power on a one-for-one basis) representing approximately 61% of Capital Power L.P. Each exchangeable L.P. unit is accompanied by a special voting share of Capital Power which entitles the holder to a vote at Capital Power shareholder meetings, subject to the restriction that such voting shares held by EPCOR must at all times represent not more than 49% of the votes attached to all Capital Power common shares and special voting shares together. The special shares also entitle EPCOR to elect a maximum of four out of twelve directors of Capital Power. As a result of these restrictive rights, EPCOR has significant influence, but not control, of Capital Power and therefore uses the equity method to account for its investment in Capital Power.

The investment was initially recorded at the cost of the net assets of the power generation business retained by EPCOR in the form of its initial 72% interest in Capital Power. The investment is reduced by subsequent sales of any portion of the investment in Capital Power, distributions paid by Capital Power on EPCOR's investment, and any other than temporary asset impairments. The investment is increased to recognize the Company's share of earnings of Capital Power. In addition, there is approximately \$18 million of accumulated losses associated with the investment in Capital Power included in accumulated other comprehensive loss at December 31, 2010 (2009 - \$16 million). On any sale of exchangeable L.P. units of Capital Power, the Company will recognize a portion of these losses in proportion to the remaining interest sold.

During December 2010, through a secondary public offering and in accordance with agreements with Capital Power and a syndicate of underwriters, the Company sold 9.2 million exchangeable L.P. units, for net proceeds of \$212 million (after fees and other incremental disposition costs) and the Company recorded a loss on sale of \$33 million including \$2 million from accumulated other comprehensive losses.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

As a result of the disposition, the Company's interest in Capital Power decreased to 61% at December 31, 2010 (2009 - 72%)

The investment in Capital Power L.P. is detailed as follows:

	2010	2009
Opening balance	\$ 1,481	\$ -
Initial investment		1,415
Sale of a portion of the investment	(243)	-
Equity share of net income	88	68
Equity share of other comprehensive income	(4)	16
Capital Power distributions	(87)	(18)
	\$ 1,235	\$ 1,481

Summarized financial information of Capital Power L.P.:

	2010	2009
Revenues	\$ 1,742	\$ 1,000
Net income attributable to partners	118	98

	2010	2009
Total assets	\$ 5,242	\$ 5,031
Total debt	\$ 2,053	\$ 1,771
Total other liabilities	677	693
Total liabilities	2,730	2,464
Non-controlling interest	503	571
Equity attributable to partners	2,009	1,996
Total liabilities and equity ⁽¹⁾	\$ 5,242	\$ 5,031

⁽¹⁾ Includes the Company's investment in the debt and equity of Capital Power L.P.

4. Sale of power generation business:

In May 2009, EPCOR announced its plans to create Capital Power (consisting of Capital Power Corporation and its subsidiaries, including Capital Power L.P.), a power generation company that is headquartered in Edmonton. The final prospectus for the initial public offering of 21,750,000 common shares of Capital Power, at \$23.00 per common share, was filed with securities regulators in Canada on June 25, 2009. The initial public offering closed in early July 2009.

Through a series of transactions, EPCOR sold substantially all of its power generation assets, net of certain liabilities, and related operations including its 30.6% interest in CPILP, to Capital Power effective early July 2009. The assets and related operations were previously included in EPCOR's Generation and Energy Services segments. EPCOR also entered into various agreements with Capital Power to provide for certain aspects of the separation of the power generation business from EPCOR, to provide for the continuity of operations and services and to govern the ongoing relationships between the two groups of entities.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

The total consideration for the sale consisted of \$468 million of cash (net of offering costs), 56.6 million exchangeable L.P. units of Capital Power L.P. and \$896 million in unsecured long-term loans receivable from Capital Power L.P. In addition, EPCOR holds one special limited voting share in Capital Power providing the right to vote separately as a class in connection with certain amendments to the articles of Capital Power, including an amendment to change or permit the change of the location of the head office of Capital Power from the City.

Effectively, EPCOR sold 28% of its interest in the power generation business and through its equity investment in Capital Power, retained a 72% interest in that business. The difference between EPCOR's net carrying amount of \$2,855 million representing its investment in the power generation business and the consideration received resulted in a loss on sale of \$92 million including \$37 million in direct expenses incurred in connection with the sale plus a \$38 million income tax charge related to net future income tax assets that are not realizable by the Company as a result of the sale. Unrealized losses related to EPCOR's 28% interest in the power generation business that was sold, previously recorded in accumulated other comprehensive income (AOCI), were recognized in net income in the fourth quarter of 2009.

Investment in power generation business on 100% basis	
Consideration (before deducting offering costs)	\$ 2,699
Carrying amount of investment in power generation business prior to sale	2,855
Carrying amount of investment in excess of consideration	156
Loss on sale of power generation business	
For 28% interest disposed of –	
carrying amount of investment in excess of consideration	43
Losses reclassified from AOCI to net income	12
Direct expenses (including offering costs)	37
Loss on sale before income taxes	92
Income taxes	38
Loss on sale after income taxes	\$ 130

Immediately following completion of the transactions, EPCOR held 56.6 million exchangeable L.P. units of Capital Power L.P. (exchangeable for common shares of Capital Power on a one-for-one basis) representing approximately 72% of Capital Power L.P., while Capital Power held the remaining 28%.

Effective July 2009, income from CPILP is included in the income from EPCOR's equity investment in Capital Power as EPCOR no longer consolidates CPILP in its consolidated financial statements. CPILP is a subsidiary of Capital Power.

5. Other acquisitions and disposals:

(a) Acquisition of potable water and wastewater treatment plant assets:

In October 2009, the Company acquired potable water and wastewater treatment plant assets from Suncor Energy for approximately \$100 million and entered into an agreement to lease the assets to Suncor Energy for a 20-year term after which Suncor Energy has the option to purchase the assets from the Company for a specified price. In addition, the Company has agreed to operate and maintain the assets as well as design, build, finance and operate upgrades to related assets, which will remain under the ownership of Suncor Energy, over the 20-year term. The Company will be compensated for all services in this agreement through payments over the 20-year term.

(b) Transfer of Gold Bar Wastewater Treatment Plant:

On March 31, 2009, the City transferred Gold Bar Wastewater Treatment Plant (Gold Bar) to EPCOR. Gold Bar primarily handles wastewater treatment requirements for residents of Edmonton.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

The Gold Bar property, plant and equipment assets were transferred on March 31, 2009 at their carrying amounts totaling \$258 million including \$48 million of contributed assets on which EPCOR cannot earn a return. EPCOR also assumed the offsetting capital contributions associated with the \$48 million of contributed assets. Pursuant to the Gold Bar asset transfer agreement, EPCOR issued \$112 million of long-term debt to the City, being EPCOR's share of the City's debt obligations in respect of the Gold Bar assets. The remaining long-term debt bears interest at a weighted average rate of approximately 5.20%. The \$24 million difference between the amount paid and the City's carrying amount of Gold Bar is reflected as an equity contribution from the City.

In exchange for the net assets transferred, EPCOR will pay a total transfer fee of \$75 million. The estimated annual instalments remaining to be paid on the outstanding balance are as follows:

2011	\$	14
2012		12
2013		10
2014		6
2015		1
Total	\$	43

The Gold Bar assets, liabilities, revenues and expenses are reflected in the Water Services segment.

The Gold Bar Master Agreement identified that certain transfers of lands related to the Gold Bar plant would not occur until after the transfer date of March 31, 2009, pending the identification, subdivision and rezoning of Gold Bar site lands and adjacent lands owned by the City to be exchanged to meet future land requirements of both parties. EPCOR is reassessing its land requirements for the Gold Bar plant. Consequently, the subdivision, rezoning and the subsequent transfer of title by the City to EPCOR, originally anticipated to occur in 2011, is currently expected to occur after 2011. While the carrying amounts of the existing Gold Bar lands on City records is not material, the identification of lands to be exchanged may result in future payments being made by EPCOR to the City based on differentials in land values of the exchanged lands.

(c) Sale of power syndicate agreement

In June 2006, the Company finalized an agreement to sell its Battle River Power Purchase Arrangement and its related interest in the Battle River Power Syndicate Agreement (Battle River PSA). The agreement resulted in the sale of 75% of the Battle River PSA through to the year ended December 31, 2008.

During the first quarter of 2009, 10% of the Battle River PSA was sold. The transaction is summarized as follows:

		2009
Cash proceeds from sale	\$	47
Less net book value and costs of disposal		17
Gain on sale before income taxes		30
Less future income taxes		4
Gain on sale after income taxes	\$	26

Refundable taxes of \$6 million, which arose from the taxable capital gains on the sale of the Battle River PSA, were charged to retained earnings.

The Company's remaining interest in the Battle River PSA was sold to Capital Power as part of the sale of the power generation business in July 2009.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

6. Property, plant and equipment:

2010				
	Composite depreciation rates	Cost	Accumulated depreciation	Net book value
Water treatment and distribution	2.1%	\$ 1,920	\$ 463	\$ 1,457
Electricity				
transmission and distribution	3.0%	1,292	411	881
Retail systems and equipment	8.5%	16	7	9
Corporate information				
systems and equipment	11.7%	80	53	27
		3,308	934	2,374
Contributions:				
Water treatment and distribution	1.5%	(564)	(111)	(453)
Electricity				
transmission and distribution	2.7%	(151)	(47)	(104)
		(715)	(158)	(557)
Land	None	30	-	30
Construction work in progress	None	60	-	60
		\$ 2,683	\$ 776	\$ 1,907
2009				
	Composite depreciation rates	Cost	Accumulated depreciation	Net book value
Water treatment and distribution	2.1%	\$ 1,811	\$ 427	\$ 1,384
Electricity				
transmission and distribution	3.0%	1,179	383	796
Retail systems and equipment	10.9%	17	7	10
Corporate information				
systems and equipment	13.3%	78	47	31
		3,085	864	2,221
Contributions:				
Water treatment and distribution	1.5%	(549)	(103)	(446)
Electricity				
transmission and distribution	2.6%	(131)	(43)	(88)
		(680)	(146)	(534)
Land	None	30	-	30
Construction work in progress	None	61	-	61
		\$ 2,496	\$ 718	\$ 1,778

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

Depreciation, amortization and asset retirement accretion expense is comprised of:

	2010	2009
Depreciation on assets in service	\$ 84	\$ 142
Accretion on asset retirement obligations (note 13)	-	3
Loss (gain) on disposal of assets	(4)	2
Amortization of contributions	(12)	(13)
Amortization of contract and customer rights and other intangible assets	20	23
Amortization of PPAs	-	22
	\$ 88	\$ 179

Interest and AFUDC (note 18) capitalized to property, plant and equipment for 2010 is \$4 million (2009 - \$20 million).

7. Contract and customer rights and other intangible assets:

	2010			2009		
	Cost	Accumulated amortization	Net book value	Cost	Accumulated amortization	Net book value
Contract rights	\$ 2	\$ 1	\$ 1	\$ 2	\$ 1	\$ 1
Customer rights	71	45	26	71	40	31
Software intangibles	166	93	73	170	92	78
	\$ 239	\$ 139	\$ 100	\$ 243	\$ 133	\$ 110

8. Long-term receivables:

	2010	2009
Loans receivable from Capital Power	\$ 612	\$ 857
Other loans	44	41
	656	898
Less: current portion	237	255
	\$ 419	\$ 643

In early July 2009, EPCOR received \$896 million in long-term loans receivable from Capital Power as part of the consideration on the sale of the power generation business. The repayments of these loans effectively mirror certain long-term debt repayment obligations of EPCOR. The interest rates on the long-term loans receivable range from 5.80% to 9.00% and will be repaid at various dates extending through June 30, 2018 as shown in note 22.

9. Other assets:

	2010	2009
Carrying amount		
Net investments in leases	\$ 130	\$ 124
Floating-rate notes	42	37
Goodwill	2	2
Other	4	1
	\$ 178	\$ 164

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

Net investments in leases

In October 2009, the Company acquired potable water and wastewater treatment plant assets from Suncor Energy for approximately \$100 million and leased the assets to Suncor Energy for a 20-year term after which Suncor Energy has the option to purchase the assets from the Company for a specified price.

In another arrangement, the Company agreed to design, build, own and operate a potable water and wastewater treatment plant for Suncor Energy. The construction of the facilities was completed in 2009.

These arrangements are considered to be leases for accounting purposes. The current portion of the net investments in leases for the year ended December 31, 2010 is \$3 million (2009 – \$3 million). Financing income recognized during the year was \$11 million (2009 – \$3 million).

Floating-rate notes

At December 31, 2010, the Company held \$42 million (2009 - \$37 million) in floating-rate notes. The floating-rate notes arose from the January 2009 restructuring of the Canadian non-bank asset backed commercial paper (ABCP) market including the Company's holdings in affected ABCP.

Under the restructuring, the affected ABCP was exchanged for term floating-rate notes maturing no earlier than the scheduled termination dates of the underlying assets. The key information on EPCOR's notes is as follows:

- (i) EPCOR's allocation of floating-rate notes under the restructuring was as follows:

Pool	Series	Rating	Face amount	
MAV2	Class A-1	A	\$ 47	67%
	Class A-2	BBB	9	13%
	Class B	Unrated	2	2%
	Class C	Unrated	2	2%
MAV3	Class 34	Unrated	5	7%
	Class 35	Unrated	4	6%
	Class 36	Unrated	2	3%
			\$ 71	100%

For the Master Asset Vehicle 2 (MAV2) floating-rate pool notes, the underlying assets are anticipated to mature in January 2017. The remaining floating-rate notes come from Master Asset Vehicle 3 (MAV3) in the form of:

- (ii) Ineligible Asset Tracking notes separated into specific classes. These floating-rate notes are expected to amortize over the lives of the underlying assets which have a weighted average maturity date of 2027. In certain limited circumstances, the expected repayment dates could be longer than the expected asset lives.
- (iii) ABCP investors, including EPCOR, were paid the accumulated accrued interest, net of ABCP restructuring costs, collateral requirements and other costs, on their existing ABCP from the date of the standstill in August 2007 to the date of the restructuring. For the year ended December 31, 2010, EPCOR received \$1 million (2009 - \$5 million) of accrued interest on ABCP and interest and principal repayments on the notes.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

Goodwill

The changes in the carrying amount of goodwill are as follows:

	2010	2009
Balance, beginning of year	\$ 2	\$ 161
Power generation sale	-	(159)
	\$ 2	\$ 2

The goodwill associated with the Company's investment in CPILP was transferred to Capital Power as part of the sale of the power generation business.

10. Short-term debt:

Bank lines of credit are unsecured and are available to the Company up to an amount of \$590 million, comprised of committed amounts of \$500 million as described in note 11 and uncommitted amounts of \$90 million. Letters of credit totaling \$135 million (2009 - \$99 million) have been issued under these facilities as described in note 27. Amounts borrowed, and letters of credit issued, if any, under these facilities which are not payable within one year are classified as long-term debt.

The Company's commercial paper program has an authorized capacity of \$500 million and an issuance limit of \$225 million under the committed credit facilities. Outstanding commercial paper at December 31, 2010 was nil (December 31, 2009 - nil).

11. Long-term debt:

	Effective Interest Rate	2010	2009
Obligation to the City, net of sinking fund (note 20):			
Due in 1-5 years at 9.31% ¹ (2009 - 9.72% ¹)	10.52%	\$ 35	\$ 64
Due in 6-10 years at 8.50% ¹ (2009 - 8.50% ¹)	11.04%	51	57
Due in 11-15 years at 7.01% ¹ (2009 - 7.01% ¹)	7.01%	23	24
Due in 16-25 years at 5.06% ¹ (2009 - 5.21% ¹)	5.36%	99	106
		208	251
Debentures, at 6.95%, due in 2010	7.12%	-	200
Debentures, at 6.60%, due in 2011	6.88%	200	200
Debentures, at 6.75%, due in 2016	6.94%	130	130
Debentures, at 5.80%, due in 2018	6.03%	400	400
Debentures, at 6.80%, due in 2029	7.05%	150	150
Debentures, at 5.65%, due in 2035	5.88%	200	200
Debentures, at 6.65%, due in 2038	6.83%	200	200
Debentures, at 5.75%, due in 2039	5.88%	200	200
		1,688	1,931
Less: Current portion		219	225
Deferred debt issue costs		13	14
		\$ 1,456	\$ 1,692

¹ Weighted average coupon rate on gross principal balance outstanding

Obligation to the City

Debentures were issued, on behalf of the Company, pursuant to the City Bylaw authorization. The outstanding debentures are a direct, unconditional obligation of the City. The Company's obligation to the City matches the City's obligation pursuant to the debentures. The portion of the 8.50% debentures, maturing in the year 2018 and totaling \$51 million, rank as subordinated debt. In the event of default on

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

other interest obligations, the coupon and sinking fund payments on the subordinated debt may be deferred for a period of up to five years, not exceeding the maturity date. If still in default at the end of five years, all unpaid payments plus accrued interest thereon may be repaid by issuing common shares to the City. Except for the subordinated debt, the obligation to the City will rank at least equal to all future debt that may be issued by the Company.

The Company makes annual contributions into the sinking fund of the City pertaining to certain debenture issues. These payments constitute effective settlement of the respective debt as the sinking fund accumulates to satisfy the underlying debenture maturity. For any specific City debenture with sinking fund requirements, the payment obligation ceases on maturity of the debenture.

On March 31, 2009, the City transferred Gold Bar to EPCOR. Pursuant to the Gold Bar asset transfer agreement, EPCOR issued \$112 million of long-term debt to the City representing EPCOR's proportionate share of the City's debt obligations in respect of Gold Bar assets. The remaining long-term debt bears interest at a weighted average rate of approximately 5.20%.

Debentures

The Debentures are unsecured direct obligations of the Company and, subject to statutory preferred exemptions, rank equally with all other unsecured and unsubordinated indebtedness of the Company. The debentures are redeemable by the Company prior to maturity at the greater of par and a price specified under the terms of the debenture.

Revolving extendible credit facilities

A \$500 million extendible syndicated bank revolving credit facility, consisting of two tranches of \$250 million each, both committed to 2013 (extended to 2014 in February 2011) is available to the Company. At December 31, 2010, the Company had nil outstanding under this facility (2009 – nil), other than \$72 million of letters of credit issued against it, which is extendible beyond 2010 (2009 – \$95 million).

12. Other non-current liabilities:

	2010	2009
Asset retirement obligations (note 13)	\$ 4	\$ 14
Employee future benefit liabilities	22	21
Gold Bar transfer fee payable	29	43
Other	3	3
	\$ 58	\$ 81

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

13. Asset retirement obligations:

	2010	2009
Balance, beginning of year	\$ 19	\$ 112
Liabilities incurred	-	4
Liabilities settled	(4)	(6)
Asset retirement accretion expense	-	3
Foreign currency revaluation	-	(1)
Revision in estimated cash flows to settle asset retirement obligation ¹	(4)	-
Sale of power generation assets	-	(93)
	11	19
Less: current portion in accounts payable and accrued liabilities	7	5
	\$ 4	\$ 14

¹ Included in Depreciation, amortization and asset retirement expense in the statement of income and as part of Loss (gain) on disposal of assets in note 6.

The Company estimates the undiscounted amount of cash flow required to settle its asset retirement obligations (ARO) is approximately \$11 million (2009 - \$19 million), calculated using inflation rates of 2.0%. The expected timing for settlement of the obligations is between 2011 and 2012. The carrying amount of the ARO has not been discounted as the majority of the asset retirement obligation relates to a project in the decommissioning stage.

14. Non-controlling interests:

Non-controlling interests associated with net income are as follows:

	2010	2009
Non-controlling interests in CPILP	\$ -	\$ 19
Preferred share dividends paid by subsidiary companies	-	3
	\$ -	\$ 22

As a result of the sale of the power generation business in July 2009, the Company has no non-controlling interests to reflect on the consolidated balances sheets at December 31, 2010 and 2009.

15. Share capital and contributed surplus:

Authorized:

Unlimited number of voting common shares without nominal or par value.

Issued:

Three common shares for nominal value to the City.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

16. Accumulated other comprehensive loss

The components of accumulated other comprehensive loss are summarized as follows:

	2010	2009
Equity in other comprehensive income of Capital Power ¹	\$ 8	\$ 16
Unrealized losses on derivative instruments designated as cash flow hedges ²	(11)	(13)
Unrealized loss in self-sustaining foreign operations ³	(54)	(65)
Non-controlling interests ³	39	46
	\$ (18)	\$ (16)

¹ Net of income tax expense of nil (2009 – \$2 million)

² Net of income tax recovery of \$4 million (2009 – \$4 million).

³ Net of income tax expense of nil (2009 – nil).

17. Change in non-cash operating working capital:

	2010	2009
Accounts receivable	\$ (36)	\$ 45
Income taxes recoverable	2	(3)
Inventories	1	(4)
Prepaid expenses	(1)	(3)
Accounts payable and accrued liabilities	29	(88)
Income taxes payable	6	(28)
Other current liabilities	4	-
	\$ 5	\$ (81)

Relating to:

Operating activities	\$ 9	\$ (54)
Investing activities	(4)	(27)
	\$ 5	\$ (81)

18. Net financing expenses:

	2010	2009
Interest on long-term debt	\$ 132	\$ 160
Interest on short-term debt and other financing costs	4	9
Fair value changes on financial instruments	(6)	1
Capitalized interest and AFUDC	(4)	(20)
Other	1	9
	\$ 127	\$ 159

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

19. Income taxes:

	2010	2009
Current income taxes	\$ 8	\$ 26
Future income taxes (reductions)	(1)	1
	\$ 7	\$ 27

Income taxes differ from the amounts that would be computed by applying the federal and provincial income tax rates as follows:

	2010	2009
Net income before income taxes and non-controlling interests	\$ 140	\$ 174
Statutory income tax rates	28.00%	29.00%
Income taxes at statutory rates	39	50
Increase (decrease) resulting from:		
Income exempt from income taxes at statutory rates	(41)	(22)
Unrecognized future income tax assets	17	7
Non-taxable portion of capital items	(6)	36
Non-taxable amounts	-	(3)
Adjustment for enacted changes in income tax laws and rates and other tax rate differences	(2)	25
Elimination of inside basis difference due to disposal of investments	-	(52)
Other	-	(14)
	\$ 7	\$ 27

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

The tax effects of temporary differences that give rise to significant portions of the future income tax assets and future income tax liabilities are presented below:

	2010	2009
Future income tax assets:		
Losses carried forward	\$ 78	\$ 84
Property, plant and equipment – differences in net book value and undepreciated capital cost	1	-
Asset retirement obligations	17	19
Contract and customer rights and other intangible assets	8	8
Other	1	1
	105	112
Future income tax liabilities:		
Investment in partnership	41	46
Deferred income from partnership	8	10
Property, plant and equipment – differences in net book value and undepreciated capital cost	1	1
Asset retirement obligation assets	6	6
Contract and customer rights and other intangible assets	6	7
Other	2	1
	64	71
Net future tax assets	\$ 41	\$ 41
Presented on the balance sheet as follows:		
Current assets	\$ 1	\$ 1
Non-current assets	41	40
Non-current liabilities	1	-
	\$ 41	\$ 41

At December 31, 2010, the Company has non-capital losses carried forward of approximately \$251 million (2009 - \$177 million) which expire between 2013 and 2030. The Company also has capital losses of approximately \$498 million (2009 - \$622 million) which carry forward indefinitely. There are non-capital losses available to be carried forward of \$131 million (2009 - \$38 million), capital losses available to be carried forward of \$279 million (2009 - \$403 million) and other deductible temporary differences of \$6 million (2009 - \$8 million) for which no tax benefit has been recognized.

In 2009, there was a refundable tax charge of \$6 million recorded in retained earnings arising from the sale of Battle River PSA as described in note 5c.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

20. Fair value and classification of financial assets and liabilities:

Accounts receivable are classified as loans and receivables; short-term debt, accounts payable and accrued liabilities, and other current liabilities and non-current liabilities are classified as other financial liabilities, all of which are measured at amortized cost and their fair values are not materially different from their carrying amounts due to their short-term nature. The Company's beneficial interest in the sinking fund related to the City debentures is classified as available-for-sale.

The classification, carrying amounts and fair values of the Company's other financial instruments at December 31, 2010 and December 31, 2009 respectively are summarized as follows:

Financial asset or liability	Classification	2010		2009	
		Carrying amount	Fair value	Carrying amount	Fair value
Other assets					
Cash and cash equivalents	Held for trading	\$ 104	\$ 104	\$ 11	\$ 11
Floating-rate notes	Held for trading	42	42	37	37
Net investments in leases (including current portion)	Loans and receivables	133	171	127	143
Long-term receivables (including current portion)	Loans and receivables	656	720	898	955
Long-term debt (including current portion)	Other financial liabilities	1,675	1,908	1,917	2,058

Fair value hierarchy

The financial instruments of the Company that are recorded at fair value have been classified into levels using a fair value hierarchy. A Level 1 valuation is determined by unadjusted quoted prices in active markets for identical assets or liabilities. A Level 2 valuation is based upon inputs other than quoted prices included in Level 1 that are observable for the instrument either directly or indirectly. A Level 3 valuation for the assets or liabilities is not based on observable market data.

Financial instruments were classified as follows:

Financial instrument	2010			Total
	Level 1	Level 2	Level 3	
Cash and cash equivalents	\$ 104	\$ -	\$ -	\$ 104
Floating-rate notes	-	42	-	42

Financial instrument	2009			Total
	Level 1	Level 2	Level 3	
Cash and cash equivalents	\$ 11	\$ -	\$ -	\$ 11
Floating-rate notes	-	37	-	37

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

Cash and cash equivalents

Under GAAP, the fair value of cash and cash equivalents is determined by unadjusted quoted prices from active markets.

Floating-rate notes

There are limited observable market prices for the floating-rate notes as at the balance sheet date. Accordingly, EPCOR has estimated the fair value using a probability-weighted discounted cash flow approach based on the assumed credit ratings and potential ratings actions on the applicable floating-rate notes, observable interest rates and credit spreads for estimating future interest payments and applicable discount rates, the cost of margin call facilities, estimated recovery periods based on the estimated lives of the underlying assets associated with the floating-rate notes and ranges of recoverability based on publicly available default statistics for credit-rated entities. In estimating future cash flows from the floating-rate notes, the Company assumed that it will earn interest at rates ranging from 0.62% to 1.32% (weighted average rate of 0.71%) (2009 - 0.00% to 0.51%; weighted average rate of 0.08%) depending on the floating-rate note series, taking into account margin funding. The future cash flows were discounted at rates ranging from 4.39% to 49.74% (weighted average rate of 11.00%) (2009 - 4.93% to 44.22%; weighted average rate of 13.20%), depending on the floating-rate note series, over 6.1 years to 11.0 years (weighted average amortization period of 5.7 years) (2009 - 7.1 years to 25.0 years; weighted average amortization period of 8.5 years), taking into account the assumed credit spreads and mortality rates. In estimating the future cash flows from the floating-rate notes, the Company assumed that cash flows from MAV2 Class B and Class C floating-rate notes would be nil due to their subordination to the MAV2 Class A floating-rate notes.

On January 21, 2009, the Company recorded the exchange of ABCP for floating-rate notes at the estimated fair value of the ABCP on that date. The fair value of the floating-rate notes increased by \$5 million for the year ended December 31, 2010 (2009 – \$5 million decrease in fair value). Under GAAP, the fair value of the floating-rate notes is determined by inputs that are not based on observable market data.

The estimate of fair value of the floating-rate notes is subject to significant risks and uncertainties including the timing and amount of future cash payments, market liquidity, the quality and tenor of the underlying assets and instruments underlying the floating-rate notes including the possibility of margin calls, and the future market for the floating-rate notes. Accordingly, the fair value estimate of the floating-rate notes may change materially. As the estimate of fair value of the floating-rate notes is not solely based on available observable market data, changing one or more of the assumptions to other reasonably possible alternative assumptions could change the fair value and correspondingly, net income. The sensitivity of the estimated fair value to changes in key valuation assumptions, holding all other assumptions constant, is as follows:

Assumption	Change	Impact on estimated fair value and net income
Amortization term	+/- 1 year	-/+ \$1
Interest rate on floating-rate notes or cost of margin call facilities	+/- 1.00%	+/- \$4
Credit ratings downgrade (increase in loss probability and losses realized)	3 notch downgrade	- \$3 to -\$5

Refer to note 9 for additional disclosure on the Company's floating-rate notes.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

Net investments in leases

The fair values of the Company's net investments in leases are based on the estimated interest rates implicit in comparable lease arrangements or loans plus an estimated credit spread based on the counterparty risk as at December 31, 2010 and December 31, 2009.

Long-term receivables

The fair value of the Company's unsecured long-term receivable is based on a current yield for the Company's receivable as at December 31, 2010 and 2009. This yield is based on an estimated credit spread for Capital Power over the yields of long-term Government of Canada bonds that have similar maturities to the Company's receivable. The estimated credit spread is based on Capital Power's indicative spread as published by independent financial institutions.

Long-term debt and Sinking Fund

The fair value of the Company's long-term debt is based on determining a current yield for the Company's debt as at December 31, 2010 and 2009. This yield is based on an estimated credit spread for the Company over the yields of long-term Government of Canada bonds that have similar maturities to the Company's debt. The estimated credit spread is based on the Company's indicative spread as published by independent financial institutions. Long-term debt (including the current portion) includes City debentures which are offset by payments made by the Company into the Sinking Fund. The Company's beneficial interest in the Sinking Fund is not quoted in an active market and therefore recorded at cost.

21. Derivative instruments and hedge accounting:

Prior to the sale of the power generation business in July 2009, derivative financial and non-financial instruments were held for the purpose of energy purchases, merchant trading or financial risk management. Subsequent to the sale of the power generation business in July 2009, derivative financial instruments may be held for the purpose of energy purchase or financial risk management. At December 31, 2010 and 2009, the Company held no derivative financial instruments.

Unrealized and realized pre-tax gains and losses on derivative instruments recognized in other comprehensive income and net income were as follows:

	2010		2009	
	Unrealized gains	Realized gains (losses)	Unrealized gains (losses)	Realized gains (losses)
Energy cash flow hedges	\$ -	\$ -	\$ 16	\$ (17)
Energy non-hedges	-	-	9	(32)
Foreign exchange non-hedges	-	-	13	4
Losses realized in net income upon sale of power generation business	-	-	-	(12)

Realized gains and losses disclosed above relate only to financial derivative instruments. Realized gains and losses on non-financial derivative instruments are recorded in energy revenues or energy purchases and fuel, as appropriate. With the sale of the power generation business in July 2009, the derivative instruments associated with the unrealized gains and losses were transferred to Capital Power (see note 4).

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

22. Risk management

Risk management overview

The Company is exposed to a number of different financial risks, arising from business activities and its use of financial instruments, including market risk, credit risk, and liquidity risk. The Company's overall risk management process is designed to identify, manage and mitigate business risk which includes, among other risks, financial risk. Enterprise risk management is overseen by the Board of Directors and senior management is responsible for fulfilling objectives, targets, and policies approved by the Board of Directors. The Director of Risk, Assurance and Advisory Services, provides a quarterly assessment to the Board of Directors on enterprise risk. Risk management strategies, policies, and limits are designed to help ensure the risk exposures are managed within the Company's business objectives and risk tolerance. The Company's financial risk management objective is to protect and minimize volatility in earnings and cash flow.

Financial risk management including foreign exchange risk, interest rate risk, liquidity risk, and the associated credit risk management, is carried out by a centralized Treasury function in accordance with applicable policies. The Audit Committee of the Board of Directors, in its oversight role, performs regular and ad-hoc reviews of risk management controls and procedures to help ensure compliance.

Risks related to investment in Capital Power

Significant reliance is placed on the capacity of Capital Power to honor its back-to-back debt obligations with EPCOR. While EPCOR has a significant economic interest in Capital Power, EPCOR does not control Capital Power. Should Capital Power fail to satisfy these obligations, EPCOR's capacity to satisfy its debt obligations would be reduced and EPCOR would need to satisfy its own debt obligations by other means.

Capital Power has indemnified EPCOR for any losses arising from its inability to discharge its liabilities, including any amounts owing to EPCOR in relation to the long-term loans receivable.

In addition, EPCOR relies on the cash flow from Capital Power partnership distributions as one of the Company's funding sources. The Capital Power distributions are paid at the discretion of the general partner of Capital Power L.P., which EPCOR does not control. There can be no assurance that Capital Power L.P. will continue to pay distributions at current levels as the distributions may be reduced or eliminated entirely in the future.

Underlying these risks are the specific business risks of Capital Power. EPCOR's ability to manage these risks is limited. EPCOR, by virtue of its holdings of exchangeable units in Capital Power L.P., has four elected directors on the Board of Capital Power. This does give EPCOR some influence over certain of the operating and strategic decisions made by Capital Power, including risk management.

Market risk

Market risk is the risk of loss that results from changes in market factors such as commodity prices, foreign currency exchange rates, interest rates, and equity prices. The level of market risk to which the Company is exposed at any point in time varies depending on market conditions, expectations of future price or market rate movements and the composition of the Company's financial assets and liabilities held, non-trading physical asset and contract portfolios, and trading portfolios.

To manage the exposure related to changes in market risk, the Company may use various risk management techniques including derivative instruments. Derivative instruments may include forward contracts, fixed-for-floating swaps (or contracts-for-differences), and option contracts. Such derivative instruments may be used to establish a fixed price for an energy commodity, an interest-bearing obligation or an obligation denominated in a foreign currency.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

The sensitivities provided in each of the following risk discussions disclose the effect of reasonably possible changes in relevant prices and rates on net income at the reporting date. The sensitivities are hypothetical and should not be considered to be predictive of future performance or indicative of earnings on these contracts. The Company's actual exposure to market risks is constantly changing as the Company's portfolio of debt, foreign currency and commodity contracts changes. Changes in fair values or cash flows based on market variable fluctuations cannot be extrapolated since the relationship between the change in the market variable and the change in fair value or cash flows may not be linear. In addition, the effect of a change in a particular market variable on fair values or cash flows is calculated without considering interrelationships between the various market rates or mitigating actions that would be taken by the Company.

Commodity price risk

The Company's direct commodity exposure is limited to energy procurement and given the regulated structure of the RRT business, commodity exposures are not material.

Foreign exchange risk

The Company is exposed to foreign exchange risk on foreign currency denominated forecasted transactions, and firm commitments, and monetary assets and liabilities denominated in a foreign currency and on its net investments in foreign entities.

The Company's foreign exchange management policy attempts to minimize economic and material transactional exposures arising from movements in the Canadian dollar relative to the U.S. dollar or other foreign currencies. The Company's direct exposure to foreign exchange risk arises on capital expenditure commitments denominated in U.S. dollars or other foreign currencies. The Company coordinates and manages foreign exchange risk centrally, by identifying opportunities for naturally occurring opposite movements and then dealing with any material residual foreign exchange risks.

The Company may use foreign currency forward contracts to fix the functional currency of its non-functional currency cash flows thereby reducing its anticipated U.S. dollar denominated transactional exposure. The Company looks to limit foreign currency exposures as a percentage of estimated future cash flows. The direct foreign currency exposures of the Company at December 31, 2010 are not material.

Interest rate risk

The Company is exposed to changes in interest rates on its cash and cash equivalents, and floating-rate short-term and long-term loans and obligations. The Company is exposed to interest rate risk from the possibility that changes in the interest rates will affect future cash flows or the fair values of its financial instruments. In some circumstances, floating-rate funding may be used for short-term borrowings and other liquidity requirements. At December 31, 2010 and 2009, all long-term debt was fixed rate. The Company may also use derivative instruments to manage interest rate risk. At December 31, 2010 and December 31, 2009, the Company did not hold any interest rate derivative instruments.

Assuming that the amount and mix of fixed and floating-rate loans and net debt remains unchanged from that held at December 31, 2010, a 100 basis point increase or decrease to interest rates would have no impact on full year net income (2009 – it would have no impact on full year net income) and would have no direct impact on other comprehensive income in either year. The effect on net income does not consider the effect of an overall change in economic activity that would accompany such an increase or decrease in interest rates.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

Credit risk

Credit risk is the possible financial loss associated with the inability of counterparties to satisfy their contractual obligations to the Company. The Company's counterparty credit risk management policy is approved by the Board of Directors and the associated procedures and practices are designed to manage the credit risks associated with the various business activities throughout the Company. Credit and counterparty risk management procedures and practices generally include assessment of individual counterparty creditworthiness and establishment of exposure limits prior to entering into a transaction with the counterparty. Exposures and concentrations are subsequently monitored and are regularly reported to senior management. Creditworthiness continues to be evaluated after transactions have been initiated, at minimum, on an annual basis. To manage and mitigate credit risk, the Company employs various credit mitigation practices such as master netting agreements, pre-payment arrangements from retail customers, credit derivatives and other forms of credit enhancements including cash deposits, parent company guarantees, and bank letters of credit.

Maximum credit risk exposure

The Company's maximum credit exposure was represented by the carrying amount of the following:

	2010	2009
Cash and cash equivalents	\$ 104	\$ 11
Accounts receivable ¹	279	243
Floating-rate notes	42	37
Long-term receivables	656	898
Net investments in leases	133	127
Financial guarantees to third parties	18	28
	\$ 1,232	\$ 1,344

¹ The Company's maximum exposure related to accounts receivable by major credit concentration is comprised of maximum exposures of \$234 million (2009 - \$204 million) related to rate-regulated customer balances.

This table does not take into account collateral held. At December 31, 2010, the Company held cash deposits of \$36 million (2009 - \$22 million) as security for certain counterparty accounts receivable. The Company is not permitted to sell or re-pledge this collateral in the absence of default of the counterparties providing the collateral. At December 31, 2010, the Company also held other forms of credit enhancement in the form of letters of credit of \$8 million (2009 - \$1 million) and parental guarantees of \$6 million (2009 - \$1 million).

Credit quality and concentrations

The Company is exposed to credit risk on outstanding accounts receivable associated with its water and energy sales activities and agreements with the Alberta Electric System Operator (AESO) and on energy supply agreements with wholesale and retail customers. The Company is also exposed to credit risk from its cash and cash equivalents (including short-term investments), financial and non-financial derivative instruments, and long-term financing arrangements.

The credit quality of the Company's accounts receivable, by major credit concentrations, and other financial assets are approximately as follows:

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

	December 31, 2010	
	Investment grade ¹ or secured ³	Unrated
Accounts receivable and financial derivative instruments		
Rate-regulated customers ²	-	100%
Water customers	38%	62%
Cash and cash equivalents	100%	-
Loans and other long-term receivables	100%	-
Floating-rate notes	82%	18%

	December 31, 2009	
	Investment grade ¹ or secured ³	Unrated
Accounts receivable and financial derivative instruments		
Rate-regulated customers ²	-	100%
Water customers	42%	58%
Cash and cash equivalents	100%	-
Loans and other long-term receivables	100%	-
Floating-rate notes	81%	19%

¹ Credit ratings are based on the Company's internal criteria and analyses, which take into account, among other factors, the investment grade ratings of external credit rating agencies when available.

² Rate-regulated customer trade receivables include distribution and transmission, water sales, rate-regulated, and default power supply receivables. Under the *Alberta Electric Utilities Act* (Alberta), the Company provides electricity supply in its service area to residential, agricultural and small commercial customers at regulated rates, and those commercial and industrial customers who have not chosen a competitive offer and consume electricity under default supply arrangements.

³ Certain accounts receivable and other financial assets are considered to have low credit risk as they are either secured by the underlying assets, secured by other forms of credit enhancements, or the counterparties are local or provincial governments.

Rate-regulated customer credit risk

Credit risk exposure for residential and commercial customers under default power and regulated water supply rates is generally limited to amounts due from customers for electricity and water consumed but not yet paid for. The Company mitigates credit risk from counterparties under default and RRT power supply rates by performing credit checks and on higher risk customers, by taking pre-payments or cash deposits. For rate-regulated customers, regulations allow for the recovery of a percentage of unforecasted credit losses through a deferral account. The Company monitors credit risk for this portfolio at the gross exposure level.

Accounts receivable and allowance for doubtful-accounts

Accounts receivable consist primarily of amounts due from retail customers including industrial and commercial customers, other retailers, government-owned or sponsored entities, regulated public utility distributors, and other counterparties. Larger commercial and industrial customer contracts and contracts-for-differences provide for performance assurances including letters of credit. For other retail customers, represented by a diversified customer base, credit losses are generally low and the Company provides for an allowance for doubtful accounts on estimated credit losses. The Company also has credit exposures to large suppliers of electricity. The Company mitigates these exposures by dealing with creditworthy

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

counterparties and, when appropriate and contractually allowed, taking back appropriate security from the supplier.

The aging of accounts receivable was:

	December 31, 2010		
	Gross accounts receivable	Allowance for doubtful accounts	Net accounts receivable
Current ¹	\$ 242	\$ -	\$ 242
Outstanding 30 to 60 days	12	-	12
Outstanding 61 to 90 days	5	1	4
Outstanding more than 90 days ²	23	2	21
Total	\$ 282	\$ 3	\$ 279

	December 31, 2009		
	Gross accounts receivable	Allowance for doubtful accounts	Net accounts receivable
Current ¹	\$ 208	\$ -	\$ 208
Outstanding 30 to 60 days	10	-	10
Outstanding 61 to 90 days	5	2	3
Outstanding more than 90 days ²	23	1	22
Total	\$ 246	\$ 3	\$ 243

¹ Current amounts represent accounts receivable outstanding from zero to 30 days. Amounts outstanding more than 30 days are considered past due.

² Includes \$21 million (2009 - \$17 million) which is subject to regulatory approval prior to collection but has low associated credit risk.

Bad debt expense, exclusive of recoveries, of \$5 million recognized in the year (2009 - \$4 million) relates to customer amounts that the Company determined would not be fully collectable. Allowances for doubtful accounts are determined by each business unit, within each operating segment, considering the unique factors of the business unit's accounts receivable. Allowances and write-offs are determined by each business unit, either by applying specific risk factors to customer groups' aged balances in accounts receivable or by reviewing material accounts on a case-by-case basis. Reductions in accounts receivable and the related allowance for doubtful accounts are recorded when the Company has determined that recovery is not possible.

The changes in the allowance for doubtful accounts were as follows:

	2010	2009
Balance, beginning of year	\$ 3	\$ 6
Transfer with sale of power generation business	-	(2)
Allowance of receivables	5	4
Receivables written off	(6)	(6)
Recovery of receivables	1	1
Balance, end of year	\$ 3	\$ 3

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

At December 31, 2010, the Company held \$18 million (2009 - \$16 million) of customer deposits for the purpose of mitigating the credit risk associated with accounts receivable from residential and business customers.

At December 31, 2010, there was no provision for credit losses associated with accounts receivable from treasury-counterparties as all balances are considered to be fully collectable.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company's liquidity is managed centrally by the Treasury function. The Company manages liquidity risk through regular monitoring of cash and currency requirements by preparing short-term and long-term cash flow forecasts and also by matching the maturity profiles of financial assets and liabilities to identify financing requirements. The financing requirements are addressed through a combination of committed and demand revolving credit facilities, public or private debt financings, or sale of investment in Capital Power.

As at December 31, 2010, the Company had undrawn and committed bank credit facilities of \$428 million, (December 31, 2009 - \$155 million) which are committed for at least 2 years. The Company has a long-term debt rating of BBB+ and A (low), assigned by Standard and Poor's and DBRS Limited, respectively.

In addition, the Company has in place a Canadian shelf prospectus, which expires January 2, 2012, under which it may raise up to \$1 billion of debt, with maturities of not less than one year. As at December 31, 2010, the available amount remaining under the Canadian shelf prospectus was \$1 billion (December 31, 2009 - \$1 billion).

The following are the undiscounted cash flow requirements and contractual maturities of the Company's financial liabilities, including interest payments, as at December 31, 2010:

	Due within 1 year	Due 1 and 2 years	Due between 2 and 3 years	3 and 4 years	4 and 5 years	Due after more than 5 years	Total contractual cash flows
Non-derivative financial liabilities:							
Long-term debt	\$ 232	\$ 24	\$ 18	\$ 14	\$ 14	\$ 1,386	\$ 1,688
Interest payments on long-term debt	130	107	97	92	92	1,060	1,578
Accounts payable and accrued liabilities ¹	242	-	-	-	-	-	242
Other current liabilities	22	-	-	-	-	-	22
Gold Bar transfer fee liability	14	12	10	6	1	-	43
Total	\$ 640	\$ 143	\$ 125	\$ 112	\$ 107	\$ 2,446	\$ 3,573

¹ Excluding accrued interest payable of \$31 million on long-term debt.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

The following are the undiscounted cash flow requirements and contractual maturities of the Company's financial liabilities, including interest payments, as at December 31, 2009:

	Due	Due between				Due after	Total contractual cash flows
	within 1 year	1 and 2 years	2 and 3 years	3 and 4 years	4 and 5 years	more than 5 years	
Non-derivative financial liabilities:							
Long-term debt	\$ 242	\$ 232	\$ 24	\$ 18	\$ 14	\$ 1,401	\$ 1,931
Interest payments on long-term debt	150	130	107	97	92	1,152	1,728
Accounts payable and accrued liabilities ¹	209	-	-	-	-	-	209
Other current liabilities	17	-	-	-	-	-	17
Gold Bar transfer fee liability	15	14	12	10	6	1	58
Total	\$ 633	\$ 376	\$ 143	\$ 125	\$ 112	\$ 2,554	\$ 3,943

¹ Excluding accrued interest payable of \$32 million on long-term debt.

The Company has long-term loans receivable from Capital Power which match certain of the long-term debt liabilities above. The following are the undiscounted maturities of the long-term loans receivable, including current portion, from Capital Power as at December 31, 2010:

	Due	Due between				Due after	Total contractual cash flows
	within 1 year	1 and 2 years	2 and 3 years	3 and 4 years	4 and 5 years	more than 5 years	
Long-term loans receivable from Capital Power:							
	\$ 233	\$ 25	\$ 14	\$ 8	\$ 8	\$ 324	\$ 612

The following are the undiscounted maturities of the long-term loans receivable, including current portion, from Capital Power as at December 31, 2009:

	Due	Due between				Due after	Total contractual cash flows
	within 1 year	1 and 2 years	2 and 3 years	3 and 4 years	4 and 5 years	more than 5 years	
Long-term loans receivable from Capital Power:							
	\$ 245	\$ 233	\$ 25	\$ 14	\$ 8	\$ 332	\$ 857

23. Capital management:

The Company's primary objectives when managing capital are to safeguard the Company's ability to continue as a going concern, pay dividends to its shareholder in accordance with the Company's dividend policy, maintain a suitable credit rating, and to facilitate the acquisition or development of projects in Canada and the U.S. consistent with the growth strategy of the Company. The Company manages its capital structure in a manner consistent with the risk characteristics of the underlying assets. This overall objective and policy for managing capital remained unchanged in the current year from the prior comparative period.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

The Company manages capital through regular monitoring of cash and currency requirements by preparing short-term and long-term cash flow forecasts and reviewing monthly financial results. The Company matches the maturity profiles of financial assets and liabilities to identify financing requirements to help ensure an adequate amount of liquidity.

The Company considers its capital structure to consist of long-term and short-term debt net of cash and cash equivalents. The following table represents the total capital of the Company:

	2010	2009
Long-term debt (including current portion) (note 11)	\$ 1,675	\$ 1,917
Cash and cash equivalents	(104)	(11)
Net debt	1,571	1,906
Shareholder's equity	2,465	2,470
Total capital	\$ 4,036	\$ 4,376

The Company has the following externally imposed requirements on its capital as a result of its credit facilities and certain debt covenants:

- Maintenance of modified consolidated net tangible assets to consolidated net tangible assets ratio, as defined in the debt agreements, of not less than 85%;
- Maintenance of consolidated senior debt to consolidated capitalization ratio, as defined in the debt agreements, of not more than 70%;
- Maintenance of interest coverage ratio, as defined in the debt agreements, of not less than 1.75 to 1.0; and
- Limitation on debt issued by subsidiaries.

These capital restrictions are defined in accordance with the underlying agreements. For the year ended December 31, 2010, the Company complied with all externally imposed capital restrictions.

24. Related party transactions and balances:

The related party transactions described below are in the normal course of operations, and are recorded at the exchange value generally based on normal commercial rates, or as agreed to by the parties.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

The following summarizes the Company's related party transactions and balances with the City:

	2010	2009
Income statement:		
Revenues - energy and water sales	\$ 2	\$ 15
Revenues – other (a)	78	72
Operations, maintenance and administration (b)	13	10
Franchise fee, property taxes and other taxes (c)	66	62
Net financing expenses (d)	34	41
Balance sheet:		
Accounts receivable	\$ 14	\$ 15
Property, plant and equipment (e)	4	2
Accounts payable (f)	18	18
Other current liabilities (g)	14	15
Long-term debt (note 11)	208	251
Other non-current liabilities (g)	29	43
Shareholder's equity (h)	24	24

- (a) Revenues from the provision of maintenance, repair and construction services of \$72 million (2009 - \$66 million) and \$6 million for customer billing services (2009 - \$6 million).
- (b) Includes certain costs of printing services and supplies, mobile equipment services, public works and various other services pursuant to service agreements.
- (c) Franchise fee for electricity distribution operations of \$41 million (2009 - \$38 million) at 0.567 cents per kilowatt-hour (2009 - 0.5299 cents per kilowatt hour effective January 1, 2009 to October 31, 2009 and 0.580 cents per kilowatt-hour effective November 1, 2009 to December 31, 2009). Franchise fees of \$15 million (2009 - \$14 million) at 7.6% effective January 1, 2010 to March 31, 2010 and 8% effective April 1, 2010 to December 31, 2010 (2009 - 7.6%) of qualifying revenues of water services and 8% of qualifying revenues for Gold Bar. Property taxes of \$10 million (2009 - \$10 million) on property owned within the Edmonton municipal boundaries.
- (d) Interest expense on the obligation to the City at interest rates ranging from 5.20% to 9.31% (note 11).
- (e) Costs of capital construction for water distribution mains and infrastructure.
- (f) Includes \$4 million (2009 - \$3 million) for drainage and construction services and \$11 million of interest payable on long-term debt (2009 - \$12 million).
- (g) Gold Bar transfer fee payable.
- (h) Related to Gold Bar transfer (note 5b).

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

The following summarizes the Company's related party transactions and balances with Capital Power:

		2010	2009
Income statement:			
Revenues - energy sales	(a)	\$ 30	\$ 13
Revenues - financing revenues	(b)	51	30
Other revenue	(c)	6	5
Energy purchases and fuel		360	200
Operations, maintenance and administration	(d)	9	6
Equity share of income in Capital Power (note 3)		88	68
Other comprehensive income statement:			
Equity other comprehensive income (note 3)		\$ (4)	\$ 16
Balance sheet:			
Accounts receivable - accrued interest	(e)	\$ 9	\$ 9
Accounts receivable		19	4
Long-term receivable (including current portion) (note 8)		612	857
Property, plant and equipment - contributed capital	(f)	(7)	(8)
Accounts payable and accrued liabilities	(g)	46	61

(a) Includes energy distribution and transmission charges to Capital Power.

(b) Financing revenue on long-term receivable from Capital Power.

(c) Includes revenues for the provision of services by EPCOR to Capital Power under services agreements.

(d) Includes utility charges and charges for provision of services by Capital Power to EPCOR under services agreements.

(e) Accrued interest on long-term receivable from Capital Power (note 8).

(f) Contributions for the construction of aerial and underground transmission lines.

(g) Includes \$42 million (2009 - \$51 million) relating to energy purchases from Capital Power and nil (2009 - \$10 million) relating to operational cash transactions with Capital Power during the acquisition changeover period.

In addition to the transactions disclosed above, the Company recorded distributions of \$87 million from Capital Power L.P. during 2010 (six months ended December 31, 2009 - \$18 million).

Included in the Company's revenues is nil (six months ended June 30, 2009 - \$1 million) for the provision of management services by CPILP to Primary Energy Recycling Corporation under a long-term management agreement.

25. Employee future benefits:

Multiemployer defined benefit pension plan and defined contribution pension plan

Over 99% (2009 - 90%) of the Company's employees are either members of the LAPP or its registered defined contribution plan. Accordingly, the majority of the Company's pension costs and obligations are accounted for as defined contribution plans.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

Defined benefit plans

The effective date for the latest actuarial valuation the Company's supplemental pension plans was December 31, 2010. The effective date of the next valuation for funding purposes is no later than December 31, 2013 for the plan. The date used to measure the plan assets and the accrued benefit obligation was December 31, 2010. The supplemental pension plan is a non-contributory plan that is unfunded at December 31, 2010.

During 2010, the Company purchased an annuity to settle its registered defined benefit pension plan obligations. As a result of the settlement, the Company recorded a \$1 million loss after tax, which is included in Operations, maintenance and administration in the statement of income.

Pension plan benefit costs, assets and obligations

	2010	2009
Costs recognized for the years ended December 31:		
Service cost	\$ 1	\$ 2
Interest on benefit obligation	1	1
Actuarial losses	3	2
Settlement of registered defined benefit pension plan	1	-
Difference between actuarial loss recognized and actual gain on accrued benefit obligation	(3)	(2)
Defined benefit plans cost	3	3
Defined contribution plans cost	18	18
Net expense	\$ 21	\$ 21
Funded status as at December 31:		
Market value of plan assets	\$ -	\$ 1
Accrued benefit obligation	14	11
Funded status – plan deficit	(14)	(10)
Amounts not yet recognized in financial statements:		
Unamortized net losses	5	2
Accrued benefit liability recognized in financial statements	\$ (9)	\$ (8)
Expected average remaining service life in years		
– registered pension plan	N/A	11
Expected average remaining service life in years		
– supplemental pension plan	11	10

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

The accrued benefit liability is included in other non-current liabilities along with other employee future benefit liabilities. Other employee future benefit liabilities consist mainly of obligations for benefits provided to employees on long-term disability leaves.

	2010	2009
Reconciliation of accrued benefit obligation:		
Accrued benefit obligation, beginning of year	\$ 11	\$ 23
Service cost	1	2
Interest cost	1	1
Actuarial loss	3	2
Settlement of registered defined benefit obligation	(2)	-
Transfer to Capital Power	-	(17)
Accrued benefit obligation, end of year	\$ 14	\$ 11

	2010	2009
Plan assets:		
Market value of assets, beginning of year	\$ 1	\$ 9
Contributions	1	-
Settlement of registered defined benefit pension plan	(2)	-
Transfer to Capital Power	-	(8)
Market value of assets, end of year	\$ -	\$ 1

Total cash payments for pension benefits in 2010, consisting of cash contributed by the Company to the LAPP, other defined contribution and benefit plans and cash payments directly to beneficiaries for its unfunded pension plan, were \$20 million (2009 - \$20 million).

Assumptions:

The significant actuarial assumptions adopted in measuring the corporation's accrued benefit obligations were as follows:

	2010	2009
Accrued benefit obligation as at December 31		
Discount rate	5.25%	6.00%
Rate of compensation increase	4.00%	4.00%
Benefit cost for year ended December 31		
Discount rate	6.00%	5.75% and 6.25%
Rate of compensation increase	4.00%	4.00%
Expected rate of return on plan assets	N/A	6.50%

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

Information concerning the Company's registered pension plan's target asset allocation and actual asset allocation is as follows:

	2010		2009	
	Target asset allocation	Asset allocation	Target asset allocation	Asset allocation
Fixed income securities	-	-	35%	35%
Equity securities	-	-	60%	63%
Other assets	-	-	5%	2%
Total	-	-	100%	100%

26. Contingencies and commitments:

The following are EPCOR's contingency and commitments not otherwise disclosed in these financial statements:

- (a) The Company has entered into operating leases for premises.

Approximate future payments under these operating leases are as follows:

2011	\$	6
2012		11
2013		11
2014		11
2015		11
Thereafter		176
Total	\$	226

In December 2007, the Company entered into a long-term leasing agreement to lease head office commercial space in a new office tower being constructed in Edmonton. The agreement, with an effective date of January 1, 2012, extends for 20 years and provides the Company with three successive five-year renewal options. Under terms of the lease, the Company has committed to make annual payments of \$10 million for the period of January 1, 2012 through December 31, 2021 and \$11 million for the period of January 1, 2022 through December 31, 2031. The Company has negotiated to sublease approximately 34% of the space to Capital Power under the same terms and conditions as the head lease for the space.

- (b) The Company has committed to various distribution and transmission projects through 2010 and 2011, as directed by the AESO. The total estimated projects costs are \$14 million (2009 - \$41 million). The Company has incurred costs of \$8 million (2009 - \$14 million).
- (c) In June 2010, the Company entered into an agreement to acquire all of the outstanding shares of Chaparral City Water Company (Chaparral), a wholly owned subsidiary of American States Water Company, for an aggregate purchase price of US\$29 million subject to closing adjustments. Chaparral is a public utility company engaged principally in the purchase, production, distribution and sale of water to approximately 13,000 customers in the Town of Fountain Hill, Arizona and a small portion of Scottsdale, Arizona. The acquisition, which is subject to regulatory approval by the Arizona Corporation Commission, is expected to close in 2011.
- (d) The Company and its subsidiaries are subject to various legal claims that arise in the normal course of business. Management believes that the aggregate contingent liability of the Company arising from these claims is immaterial and therefore no provision has been made.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

27. Guarantees:

The Company has issued letters of credit for \$135 million (2009 - \$99 million) to meet the credit requirements of energy market participants and to meet conditions of certain service agreements.

The letters of credit include \$2 million related to prudential support provided by the Company on behalf of the purchaser of certain competitive mass-market contracts in 2004, in addition to \$16 million of guarantees issued by the Company for total prudential support at December 31, 2010 of \$18 million (2009 - \$28 million). The prudential support will be provided until November 30, 2011, unless conditions for early termination are met. The prudential support is required by the AESO and by Alberta natural gas and electricity distribution service providers that allow the purchaser to participate in the retail energy market. The AESO is an independent system operator which administers operation of the Power Pool as well as the transmission of all electrical energy through the interconnected electric system in the Province of Alberta. The Company's maximum exposure under the prudential support, based on 2010 peak usage and electricity and natural gas prices and based on maximum volumes under the energy supply agreements, is estimated at approximately \$47 million (2009 - \$70 million). The estimated maximum exposure under the prudential support agreement will vary proportionately with changes in electricity and natural gas prices. Under the terms of the security interest arrangement, the Company has established separate bank accounts under its control through which billings collected from the contracts and payments of related costs are processed. The Company's use of this cash is restricted to these purposes. At December 31, 2010, \$18 million (2009 - \$6 million) of the Company's cash resides in these bank accounts. In addition, the Company has received a \$7 million (2009 - nil) letter of credit, which is shared with another party to the security interest arrangement, from the purchaser which can be drawn on should the Company be required to make payments under the prudential support agreement. There are no known material liabilities under the prudential support agreement as at December 31, 2010.

Prior to the sale of its power generation business to Capital Power, the Company issued parental guarantees on behalf of certain power generation business subsidiaries, to meet the credit requirements of energy market participants and to meet conditions of certain service agreements. During 2010, all of the parental guarantees outstanding at December 31, 2009 (\$1,295 million) were either transferred to Capital Power or had expired.

In the normal course of business, the Company provides financial support and performance assurances including guarantees, letters of credit and surety bonds to third parties in respect of its subsidiaries. The liabilities associated with the underlying subsidiary obligations are included on the consolidated balance sheet.

The Company has no other material guarantee obligations outstanding in respect of third parties at December 31, 2010.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

28. Segment disclosures:

Prior to the sale of the power generation business in July 2009, the Company operated in the following reportable business segments, which followed the organization, management and reporting structure within the Company. Following the sale of the power generation business, the Company no longer operates directly in the Generation segment and the business activities of the Energy Services segment changed as described below. The Distribution and Transmission and Water Services segments remain unchanged. The Company operates in the following reportable business segments, which follow the organization, management and reporting structure within the Company.

Water Services

Water Services is primarily involved in the treatment and distribution of water and treatment of wastewater within Edmonton and other communities throughout Western Canada. This segment also provides complementary commercial services including the maintenance and repair of the City-owned street lighting and transportation support facilities.

Distribution and Transmission

Distribution and Transmission is involved in the rate-regulated transmission and distribution of electricity within Edmonton.

Energy Services

Energy Services is primarily involved in the provision of regulated tariff electricity service and default supply electricity services to residential and small commercial customers in Alberta. Prior to the sale of the power generation business in July 2009, Energy Services was involved in the procurement, marketing and sale of electricity and natural gas in retail and wholesale markets in Alberta, Ontario, the North Eastern U.S. and the U.S. Pacific North West.

Corporate

Corporate reflects the costs of the Company's net unallocated corporate office expenses and net financing revenues on the long-term receivable from Capital Power. Corporate holds the investment in Capital Power.

Generation

Prior to the sale of the power generation business in July 2009, Generation was involved in the development and operation of rate-regulated and non-rate-regulated electrical generation plants within Canada and the United States.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

Year ended December 31, 2010

	Distribution		Energy Services	Corporate	Intersegment Eliminations	Consolidated
	Water Services	and Transmission				
Revenues – external	\$ 370	\$ 190	\$ 861	\$ 52	\$ -	\$ 1,473
Intersegment revenues	4	125	11	-	(140)	-
Total revenues	374	315	872	52	(140)	1,473
Energy purchases and fuel	-	88	775	-	(117)	746
Operations, maintenance, administration and foreign exchange gain	224	61	43	61	(23)	366
Franchise fee, property taxes and other taxes	16	45	-	-	-	61
Depreciation, amortization and asset retirement accretion	31	36	12	9	-	88
Operating expenses	271	230	830	70	(140)	1,261
Operating income (loss) before corporate charges	103	85	42	(18)	-	212
Corporate charges (income)	31	24	12	(67)	-	-
Operating income	\$ 72	\$ 61	\$ 30	\$ 49	\$ -	\$ 212
Equity share of income of Capital Power						88
Loss on sale of portion of investment in Capital Power						(33)
Net financing expenses						(127)
Income before income taxes and non-controlling interests						\$ 140
Investment in Capital Power	\$ -	\$ -	\$ -	\$ 1,235	\$ -	\$ 1,235
Total assets	\$ 1,290	\$ 912	\$ 210	\$ 2,114	\$ (12)	\$ 4,514
Capital additions	\$ 95	\$ 114	\$ 1	\$ 8	\$ -	\$ 218
Goodwill	\$ 2	\$ -	\$ -	\$ -	\$ -	\$ 2

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

Year ended December 31, 2009							
	Distribution		Energy	Corporate	Generation	Intersegment	Consolidated
	Water	and	Services ¹			Eliminations	
	Services	Transmission					
Revenues – external	\$ 343	\$ 147	\$ 1,376	\$ 31	\$ 457	\$ -	\$ 2,354
Intersegment revenues	3	116	17	-	61	(197)	-
Total revenues	346	263	1,393	31	518	(197)	2,354
Energy purchases and fuel	-	53	1,188	-	184	(169)	1,256
Operations, maintenance, administration and foreign exchange gain	210	67	62	78	126	(28)	515
Franchise fee, property taxes and other taxes	14	49	-	1	10	-	74
Depreciation, amortization and asset retirement accretion	27	34	18	16	84	-	179
Operating expenses	251	203	1,268	95	404	(197)	2,024
Operating income (loss) before corporate charges	95	60	125	(64)	114	-	330
Corporate charges (income)	27	22	22	(94)	23	-	-
Operating income	\$ 68	\$ 38	\$ 103	\$ 30	\$ 91	\$ -	\$ 330
Gain on sale of power purchase arrangement and related transactions							30
Loss on sale of power generation business							(92)
Equity share of income of Capital Power and other							65
Net financing expenses							(159)
Income before income taxes and non-controlling interests							\$ 174
Investment in Capital Power	\$ -	\$ -	\$ -	\$ 1,481	\$ -	\$ -	\$ 1,481
Total assets	\$ 1,219	\$ 828	\$ 209	\$ 2,503	\$ -	\$ (18)	\$ 4,741
Capital additions	\$ 187	\$ 86	\$ 8	\$ 8	\$ 228	\$ -	\$ 517
Goodwill	\$ 2	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 2

¹ The Energy Services segment operating income includes \$88 million for the year ended December 31, 2009 related to the wholesale electricity and natural gas business that was sold to Capital Power.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

Geographic information:

	2010			
	Canada	U.S.	Intersegment eliminations	Total
Revenues - external	\$ 1,473	\$ -	\$ -	\$ 1,473
Intersegment revenues	-	-	-	-
Total revenues	\$ 1,473	\$ -	\$ -	\$ 1,473
Property, plant and equipment	\$ 1,907	\$ -	\$ -	\$ 1,907
Goodwill	\$ 2	\$ -	\$ -	\$ 2

	2009			
	Canada	U.S.	Intersegment eliminations	Total
Revenues - external	\$ 2,140	\$ 214	\$ -	\$ 2,354
Intersegment revenues	18	2	(20)	-
Total revenues	\$ 2,158	\$ 216	\$ (20)	\$ 2,354
Property, plant and equipment	\$ 1,778	\$ -	\$ -	\$ 1,778
Goodwill	\$ 2	\$ -	\$ -	\$ 2

Intersegment transactions occur in the normal course of operations and are recorded at exchange values which are generally at normal commercial rates. All other accounting policies of the segments are the same as those disclosed in note 2.

29. Subsequent Event

Acquisition of Arizona and New Mexico water and wastewater operations

In January 2011, the Company announced the acquisition of 100% of the stock of the Arizona- American Water Company (Arizona Water) and New Mexico-American Water Company, Inc. (New Mexico Water), both wholly-owned subsidiaries of American Water Works Company, Inc. for total consideration of US \$470 million, including the assumption of US \$10 million in debt, subject to certain adjustments. The transaction is subject to regulatory approvals in both states. Arizona Water is a regulated utility that provides water service to approximately 106,000 customers and wastewater services to approximately 51,000 customers primarily located in the Phoenix area. New Mexico Water provides water and wastewater services to the City of Clovis in eastern New Mexico, and in the greater Edgewood area near Albuquerque, serving more than 17,000 customers.

EPCOR UTILITIES INC.

Notes to Consolidated Financial Statements
(Tabular amounts in millions of dollars unless otherwise indicated)

Years ended December 31, 2010 and 2009

30. Comparative figures:

Certain of the comparative figures have been reclassified to conform with the current year's presentation.