Consolidated Financial Statements of

EPCOR UTILITIES INC.

Years ended December 31, 2012 and 2011

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 International Financial Reporting Standards. 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 5, 2013. Financial information presented elsewhere in EPCOR's 2012 Corporate Accountability 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 International Financial Reporting Standards. 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 fulfills 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 5, 2013

EPCOR UTILITIES INC.

Consolidated Financial Statements

Years ended December 31, 2012 and 2011

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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 of EPCOR Utilities Inc.

We have audited the accompanying financial statements of EPCOR Utilities Inc., which comprise the statements of financial position as at December 31, 2012 and December 31, 2011, the statements of income, comprehensive income, changes in equity and cash flows for the years ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of 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 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 audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the 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 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 financial statements.

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of EPCOR Utilities Inc. as at December 31, 2012 and December 31, 2011, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

KPMG LLP

Chartered Accountants

March 5, 2013
Edmonton, Canada

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EPCOR UTILITIES INC.

Consolidated Income Statements
(In millions of Canadian dollars)

Years ended December 31, 2012 and 2011

		2012		2011
Revenues and other income				
Revenues (note 6)	$	1,931	$	1,794
Other income (note 6)		28		39
		1,959		1,833
Expenses				
Electricity purchases and system access fees		1,006		1,076
Other raw materials and operating charges		145		115
Staff costs and employee benefits expenses (note 7)		281		236
Depreciation and amortization (note 7)		133		105
Franchise fees and property taxes		84		77
Other administrative expenses (note 7)		57		45
Foreign exchange losses (gains)		2		(9)
		1,708		1,645
Operating income		251		188
Finance expense (note 8)		(116)		(108)
Equity share of income of Capital Power (note 18)		41		90
Loss on sale of a portion of and net loss on dilutions of investment in Capital Power (note 18)		(36)		(24)
Impairment of investment in Capital Power (note 9)		(124)		-
Income before income taxes		16		146
Income tax (expense) recovery (note 10)		2		(2)
Net income for the year – all attributable to the Owner of the Company	$	18	$	144

The accompanying notes are an integral part of these consolidated financial statements

EPCOR UTILITIES INC.

Consolidated Statements of Comprehensive Income
(In millions of Canadian dollars)

Years ended December 31, 2012 and 2011

	2012	2011
Net income for the year	$ 18	$ 144
Other comprehensive income:		
Equity share of other comprehensive income (loss) of Capital Power[1] (note 18)	11	(4)
Amounts realized in net income on sale of a portion of and dilutions of investment in Capital Power [2] (note 18)	(2)	5
Unrealized gain (loss) on available-for-sale financial assets[3]	(2)	1
Unrealized gain (loss) on foreign currency translation	(1)	1
Other comprehensive income	6	3
Total comprehensive income for the year - all attributable to the Owner of the Company	$ 24	$ 147

[1] For the year ended December 31, 2012, net of income tax expense of $3 million (2011 – income tax recovery of $1 million).

[2] For the year ended December 31, 2012, net of reclassification of income tax recoveries of nil (2011 – $1 million).

[3] For the year ended December 31, 2012, net of income tax recovery of $1 million (2011 – nil).

The accompanying notes are an integral part of these consolidated financial statements

EPCOR UTILITIES INC.

Consolidated Statements of Financial Position
(In millions of Canadian dollars)

December 31, 2012 and December 31, 2011

	2012	2011
ASSETS		
Current assets:		
Cash and cash equivalents (note 11)	$ 232	$ 316
Trade and other receivables (note 12)	359	372
Inventories (note 13)	13	12
Derivatives (note 14)	-	11
	604	711
Non-current assets:		
Finance lease receivables (note 15)	125	127
Other financial assets (note 16)	383	402
Deferred tax assets (note 17)	52	43
Investment in Capital Power (note 18)	621	987
Intangible assets (notes 19 and 20)	222	104
Property, plant and equipment (note 21)	3,417	2,658
	4,820	4,321
TOTAL ASSETS	$ 5,424	$ 5,032

The accompanying notes are an integral part of these consolidated financial statements

EPCOR UTILITIES INC.

Consolidated Statements of Financial Position
(In millions of Canadian dollars)

December 31, 2012 and December 31, 2011

	2012	2011
LIABILITIES AND EQUITY		
Current liabilities:		
Trade and other payables (note 23)	$ 303	$ 264
Loans and borrowings (note 24)	14	17
Deferred revenue (note 25)	21	16
Provisions (note 26)	29	18
Derivatives (note 14)	2	-
Other liabilities (note 27)	31	34
	400	349
Non-current liabilities:		
Loans and borrowings (note 24)	1,956	1,682
Deferred revenue (note 25)	741	586
Deferred tax liabilities (note 17)	5	1
Provisions (note 26)	70	34
Other liabilities (note 27)	18	29
	2,790	2,332
Total liabilities	3,190	2,681
Equity attributable to the Owner of the Company:		
Share capital (note 28)	24	24
Accumulated other comprehensive income (note 29)	14	8
Retained earnings	2,196	2,319
Total equity	2,234	2,351
TOTAL LIABILITIES AND EQUITY	$ 5,424	$ 5,032

Commitments and contingencies (note 35)

The accompanying notes are an integral part of these consolidated financial statements

EPCOR UTILITIES INC.

Consolidated Statements of Changes in Equity
(In millions of Canadian dollars)

December 31, 2012 and 2011

		Accumulated other comprehensive income (loss)					
	Share capital (note 28)	Cash flow hedges (note 29)	Available-for-sale financial assets (note 29)	Cumulative translation account (note 29)	Investment in Capital Power (note 18, note 29)	Retained earnings	Equity attributable to the Owner of the Company
Equity at December 31, 2011	$ 24	$ (9)	$ 4	$ 1	$ 12	$ 2,319	$ 2,351
Net income for the year	-	-	-	-	-	18	18
Other comprehensive income (loss):							
Equity share of other comprehensive income of Capital Power	-	-	-	-	11	-	11
Amounts realized in net income on sale of a portion of investment in Capital Power	-	2	-	-	(4)	-	(2)
Unrealized loss on available-for-sale financial assets	-	-	(2)	-	-	-	(2)
Unrealized loss on foreign subsidiary	-	-	-	(1)	-	-	(1)
Total comprehensive income (loss)	-	2	(2)	(1)	7	18	24
Dividends	-	-	-	-	-	(141)	(141)
Equity at December 31, 2012	$ 24	$ (7)	$ 2	$ -	$ 19	$ 2,196	$ 2,234

		Accumulated other comprehensive income (loss)					
	Share capital (note 28)	Cash flow hedges (note 29)	Available-for-sale financial assets (note 29)	Cumulative translation account (note 29)	Investment in Capital Power (note 18, note 29)	Retained earnings	Equity attributable to the Owner of the Company
Equity at December 31, 2010	$ 24	$ (11)	$ 3	$ -	$ 13	$ 2,313	$ 2,342
Net income for the year	-	-	-	-	-	144	144
Other comprehensive income (loss):							
Equity share of other comprehensive loss of Capital Power	-	-	-	-	(4)	-	(4)
Amounts realized in net income on sale of a portion of and dilutions of investment in Capital Power	-	2	-	-	3	-	5
Unrealized gain on available-for-sale financial assets	-	-	1	-	-	-	1
Unrealized gain on foreign subsidiary	-	-	-	1	-	-	1
Total comprehensive income (loss)	-	2	1	1	(1)	144	147
Dividends	-	-	-	-	-	(138)	(138)
Equity at December 31, 2011	$ 24	$ (9)	$ 4	$ 1	$ 12	$ 2,319	$ 2,351

The accompanying notes are an integral part of these consolidated financial statements

EPCOR UTILITIES INC.

Consolidated Statements of Cash Flows
(In millions of Canadian dollars)

Years ended December 31, 2012 and 2011

	2012	2011
Cash flows from (used in) operating activities:		
Net income for the year	$ 18	$ 144
Reconciliation of net income for the year to cash from operating activities:		
Interest paid	(115)	(117)
Finance expense (note 8)	116	114
Income taxes paid	(4)	(13)
Income tax expense (recovery) (note 10)	(2)	2
Depreciation and amortization	133	105
Contributions received (note 25)	45	57
Deferred revenue recognized (note 25)	(20)	(12)
Gain on disposal of floating-rate notes	-	(7)
Fair value change on derivative instruments (note 14)	13	(11)
Fair value loss on floating-rate notes	-	1
Loss on sale of a portion of and on dilutions of investment in Capital Power (note 18)	36	24
Equity share of income from Capital Power (note 18)	(41)	(90)
Impairment of investment in Capital Power (note 9)	124	-
Foreign exchange gain	(2)	-
Other	3	11
	304	208
Change in non-cash operating working capital (note 30)	64	(85)
Net cash flows from operating activities	368	123
Cash flows from (used in) investing activities:		
Acquisition or construction of property, plant and equipment and other assets	(379)	(338)
Business acquisition, net of acquired cash (note 5)	(460)	(29)
Change in non-cash investing working capital (note 30)	(21)	29
Proceeds on sale of floating-rate notes	-	48
Proceeds on disposal of property, plant and equipment	7	2
Payment of Gold Bar transfer fees	(12)	(15)
Payments received on long-term receivables	25	233
Proceeds on sale of a portion of investment in Capital Power	221	215
Distributions received from Capital Power	42	60
Net cash flows from (used in) investing activities	(577)	205
Cash flows from (used in) financing activities:		
Proceeds from issuance of long-term loans and borrowings (note 33)	300	254
Repayment of long-term loans and borrowings	(35)	(232)
Provisions	1	-
Common share dividends paid	(141)	(138)
Net cash flows from (used in) financing activities	125	(116)
Increase (decrease) in cash and cash equivalents	(84)	212
Cash and cash equivalents, beginning of year	316	104
Cash and cash equivalents, end of year	$ 232	$ 316

The accompanying notes are an integral part of these consolidated financial statements

1. 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 and the United States (U.S.) with its registered head office located at 2000, 10423 - 101 Street NW, Edmonton, Alberta, Canada, T5H 0E8.

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

2. Basis of presentation

(a) Statement of compliance

These consolidated financial statements have been prepared by management in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and adopted by the Canadian Institute of Chartered Accountants (CICA). These consolidated financial statements were approved and authorized for issue by the Board of Directors on March 5, 2013.

(b) Basis of measurement

The Company's consolidated financial statements are prepared on the historical cost basis, except for its beneficial interest in the sinking fund held with the City, and its derivative financial instruments, which are measured at fair value. In addition, the Company's defined benefit pension assets are recognized as the net total of the plan assets, plus unrecognized past service cost and unrecognized actuarial losses, less unrecognized actuarial gains and the present value of the defined benefit obligation.

(c) Additional IFRS financial measure

The Company uses "operating income" as an additional IFRS financial measure. In management's opinion, the measure is a more effective indicator of the Company's and reportable business segments' operating performance than net income because it only includes items directly related to or resulting from management's operating decisions and actions.

3. Significant accounting policies

The accounting policies set out below have been applied consistently to all years presented in these consolidated financial statements unless otherwise indicated.

(a) Basis of consolidation

These consolidated financial statements include the accounts of EPCOR and its subsidiaries at December 31, 2012. Subsidiaries are fully consolidated from the date on which EPCOR obtains control, and continue to be consolidated until the date that such control ceases to exist. All intercompany balances and transactions have been eliminated on consolidation. The financial statements of the subsidiaries are prepared for the same reporting period as EPCOR, using consistent accounting policies.

(b) Business combinations and goodwill

Acquisitions of subsidiaries and businesses are accounted for using the acquisition method. The consideration for an acquisition is measured at the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of acquisition in exchange for control of the acquired business. Acquisition-related costs are expensed as incurred.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the date of acquisition. Where an acquisition involves consideration contingent on future events, any changes in the amount of consideration paid will be recognized in the income statement.

Goodwill is initially recorded at the cost of an acquisition less the fair value of the net assets of the consolidated business acquired. If the cost of an acquisition is less than the fair value of the Company's share of the net assets acquired, the difference is recognized directly in net income.

Goodwill is measured at cost less accumulated impairment losses, if any. Goodwill is tested for impairment annually at the cash generating unit level. For the purpose of impairment testing, goodwill acquired in an acquisition is, from the date of acquisition, allocated to each of the Company's cash generating units that are expected to benefit from the acquisition, irrespective of whether other assets or liabilities of the acquired business are assigned to those units.

Where goodwill forms part of a cash generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash generating unit retained.

(c) Revenue recognition

Revenue is recognized to the extent that it is probable that economic benefits will flow to the Company for the provision of goods or services and where the revenue can be reliably measured. Revenues are measured at the fair value of the consideration received or to be received, excluding discounts, rebates and sales taxes or duty.

Certain water services contracts contain multiple-deliverables arrangements. Each deliverable that is considered to be a separate unit of account is accounted for individually. Significant judgment is required to determine an appropriate allocation of the total contract value to each unit of account based on the relative fair values of each unit. If the fair value of the delivered item is not reliably measurable, then revenue is allocated based on the difference between the total arrangement consideration and the fair value of the undelivered units of account. The primary identifiable deliverables under such contracts are plant construction and project upgrades and expansions, financing or leasing of upgrades, facilities operations and facilities maintenance.

The following specific recognition criteria must also be met before revenue is recognized:

Sale of goods

Revenues from sales of electricity and water are recognized upon delivery and provision of services. These revenues include an estimate of the value of electricity and water consumed by customers billed subsequent to the reporting period.

Revenues from the sale of other goods are recognized when the products have been delivered and collectability is reasonably assured.

Provision of services

Revenues from the provision of electricity distribution and transmission services and wastewater treatment services are recognized over the period in which the service is performed and collectability is reasonably assured.

Construction contracts

Revenue from the construction of water and wastewater plants 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. These estimates result in the recognition of unbilled receivables when the revenues are earned prior to billing customers. 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 the total estimated contract revenue and expenses when approval is reasonably assured.

Revenues earned under finance leases

Finance income earned from arrangements where the Company leases water and wastewater assets to customers, are accounted for as finance leases, as described in note 3(g).

Interest income

Revenue from the financing of project 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 inception for each contract.

Interest income related to the loans receivable from Capital Power are recognized over the terms of the loans based on the interest rate applicable to each loan.

(d) 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 U.S. subsidiaries are subject to income taxes pursuant to U.S. federal and state income tax laws.

Current income taxes for the current or prior periods are measured at the amount expected to be recovered from or payable to the taxation authorities based on the tax rates that are enacted or substantively enacted by the end of the reporting period.

Deferred tax assets and liabilities are recognized for the deferred tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred 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 deferred tax assets and liabilities is recognized in income in the period that includes the date of enactment or substantive enactment.

Deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable income will be available against which those deductible temporary differences can be utilized. Deferred tax assets are assessed at each reporting date and judgment is applied to determine the likelihood that they will be realized from future taxable income and are reduced to the extent that it is no longer probable that sufficient taxable income will be available to allow all or part of the asset to be recovered.

Deferred tax liabilities are recognized for taxable temporary differences associated with investments in associates and interests in joint ventures except where the Company is able to control the timing of the reversal of the temporary differences, and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with investments in subsidiaries and interests in joint ventures are only recognized to the extent that the temporary difference will reverse in the foreseeable future and the Company judges that it is probable that there will be sufficient taxable income against which to utilize the benefits of the temporary differences. Deferred tax assets and liabilities are not recognized if the temporary difference arises from the initial recognition of goodwill arising from a business combination or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither taxable income nor accounting income.

Current and deferred taxes are recognized in profit or loss, except to the extent that they relate to items recognized directly in equity or in other comprehensive income.

(e) 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.

(f) 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 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 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.

(g) Lease arrangements

At the inception of an arrangement entered into for the use of property plant and equipment (PP&E), the Company determines whether such an arrangement is, or contains, a lease. A specific asset is the subject of a lease if fulfillment of the arrangement is dependent on the use of the specific asset. An arrangement conveys the right to use the asset if the right to control the use of the underlying asset is conveyed. Where it is determined that the arrangement contains a lease, the Company classifies the lease as either a finance or operating lease dependent on whether substantially all the risks or rewards of ownership of the asset have been transferred.

Where the Company is the lessor, finance income related to leases or arrangements accounted for as finance leases is recognized in a manner that produces a constant rate of return on the net investment in the lease. The net investment in the lease is composed of net minimum lease payments and unearned finance income. Unearned finance income is deferred and recognized in net income over the lease term.

Where the Company is the lessee, leases or other arrangements that transfer substantially all of the benefits and risks of ownership of property to the Company are classified as finance leases. Other arrangements that are determined to contain a lease are classified as operating leases. The Company currently has not entered into any arrangements as a lessee which would be classified as finance leases. Rental payments under arrangements classified as operating leases are expensed on a straight-line basis over the term of the lease.

(h) Investment in Capital Power

In these consolidated financial statements, Capital Power refers to Capital Power Corporation and its subsidiaries, including Capital Power L.P., except where otherwise noted or the context indicates otherwise.

The Company holds 28.4 million exchangeable limited partnership units of Capital Power L.P. (exchangeable for common shares of Capital Power Corporation on a one-for-one basis) which represents 29% of Capital Power. Each exchangeable limited partnership unit is accompanied by a special voting share in Capital Power Corporation which entitles the holder to a vote at Capital Power Corporation shareholder meetings, subject to the restriction that such special voting shares must at all times represent not more than 49% of the votes attached to all Capital Power Corporation common shares and special voting shares, taken together. The special voting shares also entitle EPCOR, voting separately as a class, to nominate and elect a maximum of four out of the twelve directors of Capital Power Corporation. The number of Capital Power directors which EPCOR is entitled to nominate reduces, in stages, as EPCOR’s percentage interest in Capital Power declines.

As a result, the key judgment in determining the appropriate accounting treatment for the Investment in Capital Power is that the Company does not control Capital Power's operations as it does not have the power to direct the activities of Capital Power. Accordingly, EPCOR has significant influence in Capital Power and therefore uses the equity method to account for its investment in Capital Power.

The investment in Capital Power was recognized initially at cost. The consolidated financial statements include the Company's equity share of the income and expenses and equity movements of Capital Power, after adjustments to align its accounting policies with those of the Company, from the date that significant influence exists until the date that significant influence ceases.

The Company applies judgment at each reporting date to determine whether there is objective evidence that the equity investment in Capital Power is impaired. An impairment will be recorded when the carrying amount of its investment in Capital Power exceeds its estimated recoverable amount. The recoverable amount is the higher of the investment’s fair value less costs to sell the investment, and its value in use. The fair value of the investment is based on the market price of Capital Power Corporation shares (CPX) traded on the Toronto Stock Exchange. The value in use of an asset is the present value of estimated future cash flows, applying a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

(i) Intangible assets

Intangible assets with definite lives are stated at cost, net of accumulated amortization and impairment losses, if any.

Customer rights represent the costs to acquire the rights to provide electricity services to particular customer groups for a finite period of time. Customer rights are recorded at cost at the date of acquisition. A subsequent expenditure is capitalized only when it increases the future economic benefit in the specific asset to which it relates.

Other rights represent the costs to acquire the rights, for finite periods of time, to access electricity delivery corridors, to the supply of water, to provide sewage treatment and transportation services, to withdraw groundwater and to the supply of potable water for emergency and peak purposes.

The cost of intangible software includes the cost of license acquisitions, contracted services, materials, direct labor, along with directly attributable overhead costs and borrowing costs on qualifying assets.

Amortization of the cost less estimated residual value of finite life intangible assets is recognized on a straight-line basis over the estimated economic useful lives of the assets, from the date they are available for use, as this most closely reflects the expected usage of the asset. Work in progress is not amortized. The useful economic lives, methods of amortization and residual values are reviewed annually, with any changes adopted on a prospective basis.

The estimated useful lives for intangible assets with finite lives are as follows:

Customer rights	10 – 20 years
Software assets	2 – 20 years
Other rights	50 years
Water rights	100 years

Certificates of convenience and necessity (CCN) represent the costs to acquire the exclusive rights for the Company to serve within its specified geographic areas in the U.S. for an indefinite period of time.

Gains or losses on the disposal of intangible assets are determined as the difference between the net disposal proceeds and the carrying amount of the asset, and are included within depreciation and amortization.

(j) Property, plant and equipment

PP&E are recorded at cost, net of accumulated depreciation and accumulated impairment losses, if any.

Cost includes contracted services, materials, direct labor, directly attributable overhead costs, borrowing costs on qualifying assets and decommissioning costs. Where parts of an item of PP&E have different useful lives, they are accounted for as separate items (major components) of PP&E.

The cost of major inspections and maintenance is recognized in the carrying amount of the item if the asset recognition criteria are satisfied. The carrying amount of a replaced part is derecognized. The costs of day-to-day servicing are expensed as incurred.

Gains and losses on the disposal of PP&E are determined as the difference between the net disposal proceeds and the carrying amount at the date of disposal. The gains or losses are included within depreciation and amortization.

Depreciation of cost less residual value is charged on a straight-line basis over the estimated economic useful lives of items of each depreciable component of PP&E, from the date they are available for use, as this most closely reflects the expected usage of the assets. Land and construction work in progress are not depreciated. Estimating the appropriate useful lives of assets requires significant judgment and is generally based on estimates of life characteristics of similar assets. The useful economic lives, methods of depreciation and residual values are reviewed annually with any changes adopted on a prospective basis.

The ranges of estimated useful lives used are as follows:

Water and wastewater treatment and distribution	3 – 90 years
Electricity transmission and distribution	4 – 65 years
Retail systems and equipment	2 – 65 years
Corporate information systems, equipment	2 – 20 years
Leasehold improvements	8 – 25 years

(k) Capitalized borrowing costs

The Company capitalizes interest during construction of an asset using the weighted average cost of debt incurred on the Company's external borrowings or specific borrowings used to finance qualifying assets. Qualifying assets are considered to be those that take a substantial period of time to construct.

(l) Deferred revenue

Certain assets may be acquired or constructed using non-repayable government grants or contributions from developers or customers. Non-refundable contributions received towards construction or acquisition of an item of PP&E which are used to provide ongoing service to a customer are recorded as deferred revenue and are amortized on a straight line basis over the estimated economic useful lives of the assets to which they relate.

(m) Provisions

A provision is recognized if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Each such obligation is discounted using a rate determined by reference to market interest rates at the date of the statement of financial position on high-quality debt instruments with cash flows that match the timing of the payments. The increase in the provision due to the passage of time is recognized as a financing expense over the estimated time period until settlement of the obligation.

The Company recognizes a decommissioning provision in the period in which a legal or constructive obligation is incurred. A corresponding asset for the decommissioning cost is added to the carrying amount of the associated PP&E, and is depreciated over the estimated useful life of the asset.

The Company may receive contributions from customers, homebuilders, real estate developers, and others to fund construction necessary to extend service to new areas. Certain of these contributions may be refunded for a limited period of time as new customers begin to receive service or other contractual obligations are fulfilled. The portion of contributions which are estimated to be refunded in the future are recorded as provisions. The remaining contributions are classified as deferred revenue.

(n) 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 pension plans.

The LAPP is a multi-employer 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. It is accounted for as a defined contribution plan as the LAPP is not able to provide information which reflects EPCOR's specific share of the defined benefit obligation or plan assets that would enable the Company to account for the plan as a defined benefit plan. Accordingly, the Company does not recognize its share of any plan surplus or deficit.

The Company maintains additional defined contribution and defined benefit pension plans to provide pension benefits to those employees who are not otherwise served by the LAPP, including employees of new or acquired operations. Employees participating in such defined benefit and contribution plans comprise less than 18% of total employees (2011 – less than 1%).

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

(o) Derivative financial instruments

The Company uses various risk management techniques to reduce its exposure to movements in electricity prices and foreign currency exchange rates. These include the use of derivative financial instruments such as forward contracts or contracts-for-differences. Such instruments may be used to establish a fixed price for electricity or anticipated transactions denominated in a foreign currency.

The Company sells electricity to customers under a Regulated Rate Tariff (RRT). As part of the RRT, the amount of electricity to be procured, the procurement method and electricity selling prices to be charged to these customers is determined by an Energy Price Setting Plan (EPSP). Under the EPSP commencing July 1, 2011, and unlike the previous EPSP under which the Company's electricity procurement requirements were managed by a third party, the Company manages the procurement of electricity directly. As part of the EPSP, the Company uses financial contracts-for-differences, a type of derivative financial instrument, to economically hedge the Company's exposure to fluctuations in electricity prices. Under these instruments, the Company agrees to exchange, with a single creditworthy and adequately secured counterparty, the difference between the Alberta Electric System Operator (AESO) market price and the fixed contract price for a specified volume of electricity for the forward month, all in accordance with the EPSP.

Foreign exchange forward contracts are used by the Company to manage foreign exchange exposures, consisting mainly of U.S. dollar exposures, resulting from anticipated transactions denominated in foreign currencies.

All derivative financial instruments are recorded at fair value as derivative assets or derivative liabilities on the statement of financial position, to the extent they have not been settled, with all changes in the fair value of derivatives recorded in net income.

The fair value of derivative financial instruments reflects changes in the electricity prices and foreign exchange rates. Fair value is determined based on exchange or over-the-counter price quotations by reference to bid or asking price, as appropriate, in active markets. Fair value amounts reflect management's best estimates using external readily observable market data, such as future prices, foreign exchange rates and discount rates for time value. It is possible that the assumptions used in establishing fair value amounts will differ from future outcomes and the impact of such variations could be material.

(p) Non-derivative financial instruments

Financial assets are identified and classified as either held at fair value through profit or loss, loans and receivables, or available-for-sale financial assets. Financial liabilities are classified as either held at fair value through profit or loss or other liabilities.

Financial instruments at fair value through profit or loss

Financial instruments at fair value through profit or loss comprises of cash and cash equivalents. A financial asset is classified at fair value through profit or loss if it is classified as held for trading or is designated as such upon initial recognition. The Company may designate financial instruments as held at fair value through profit or loss 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.

Financial assets held at fair value through profit or loss are measured at fair value with the changes in fair value recognized in net income.

Loans and receivables

Loans and receivables are comprised of trade and other receivables, finance lease receivables, and other financial assets.

The Company's loans and receivables are recognized initially at fair value plus directly attributable transaction costs, if any. After initial recognition, they are measured at amortized cost using the effective interest method less any impairment as described in note 3(q). The effective interest method calculates the amortized cost of a financial asset or liability and allocates the finance income or expense over the term of the financial asset or liability using an effective interest rate.

Available-for-sale financial assets

The Company's beneficial interest in the sinking fund with the City does not meet the criteria for classification in any of the previous categories and is classified as an available-for-sale financial asset and measured at fair value with changes in fair value reported in other comprehensive income until it is disposed of or becomes impaired, as described in note 3(q).

On derecognition of an available-for-sale financial asset, the cumulative gain or loss that was previously held in equity is transferred to net income.

Other liabilities

The Company's trade and other payables, loans and borrowings and other liabilities are recognized on the date at which the Company becomes a party to the contractual arrangement. Other liabilities are derecognized when the contractual obligations are discharged, cancelled or expire.

Other liabilities are recognized initially at fair value, plus directly attributable transaction costs, such as debenture discounts, premiums and issue expenses, if any. Subsequently, these liabilities are measured at amortized cost using the effective interest rate method.

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.

(q) Impairment of financial assets

The Company's financial assets held as loans and receivables or available-for-sale assets are assessed for indicators of impairment at each reporting date. An impairment loss for financial assets is recorded when it is identified that there is objective evidence that one or more events has occurred, after the initial recognition of the asset, that has had a negative impact on the estimated future cash flows of the asset and that can be reliably estimated. The objective evidence for these types of assets is as follows:

- For listed and unlisted investments in equity securities classified as available-for-sale, a significant or prolonged decline in the fair value of the investment below its cost is considered to be objective evidence of impairment.
- For all other financial assets, including finance lease receivables, objective evidence of impairment includes significant financial difficulty of the counterparty or default or delinquency in interest or principal payments.
- Trade receivables and other assets that are not assessed for impairment individually are assessed for impairment on a collective basis. Objective evidence of impairment includes the Company's past experience of collecting payments as well as observable changes in national or local economic conditions.

For financial assets carried at amortized cost, the amount of the impairment loss recognized is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the asset's original effective interest rate. If, in a subsequent period, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is adjusted.

(r) Impairment of non-financial assets

The carrying amounts of the Company's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. Non-financial assets include inventory, intangible assets and PP&E. The asset's recoverable amount is estimated if any indication of impairment exists. The asset's recoverable amount is

the higher of its fair value less costs to sell and its value in use. The fair value less costs to sell is based on estimated market values based on actual market transactions, if available, or a fair value estimation model. The value in use is the present value of estimated future cash flows using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss is recognized if the carrying amount of an asset exceeds its recoverable amount, and is recorded in the period when it is determined that the carrying amount of the asset may not be recoverable. The impairment loss will be recorded in net income for the period as the excess of the carrying amount of the asset over its recoverable amount.

At each reporting date, the Company makes an assessment as to whether there is any indication that previously incurred impairment losses have reversed. If such an indication exists, the Company estimates the asset's recoverable amount and compares it to the carrying amount, including accumulated depreciation, that would have been determined had no impairment loss been recognized. Any reversal is limited to this latter amount.

(s) Foreign currency

Transactions denominated in currencies other than the Canadian dollar are translated at exchange rates in effect at the transaction date. At each reporting date, monetary assets and liabilities denominated in foreign currencies are translated at the exchange rate in effect at the end of the reporting period. Other non-monetary assets and liabilities are not re-translated unless they are carried at fair value. Revenues and expenses are translated at average exchange rates prevailing during the period. The resulting foreign exchange gains and losses are included in net income.

On consolidation, the assets and liabilities of foreign operations that have a functional currency other than Canadian dollars are translated into Canadian dollars at the exchange rates in effect at the end of the reporting period. Revenues and expenses are translated at average exchange rates prevailing during the period. The resulting translation gains and losses are deferred and included in accumulated other comprehensive income (OCI) in the translation account. The functional currency of the Company's U.S. operations is the U.S. dollar.

(t) Investment in Heartland Transmission Project

In 2011, the Company entered into a joint venture to jointly own and control a double circuit 500 kilovolt alternating current electricity transmission line (the Heartland Transmission Project) to be constructed that will connect the 500 kilovolt electricity transmission system on the south side of the city of Edmonton to a new electricity transmission substation to be built in the Fort Saskatchewan region. The consolidated financial statements include EPCOR's relative share of the joint venture's assets, liabilities, revenue and expenses with items of a similar nature on a line-by-line basis. Unrealized gains and losses on transactions between EPCOR and the joint venture are eliminated to the extent of EPCOR's interest in the joint venture and unrealized losses are eliminated only to the extent there is no evidence of impairment.

(u) Standards and interpretations not yet applied

The following accounting standards and interpretations, which may be significant to the Company, were issued by the IASB and the International Financial Reporting Interpretations Committee (IFRIC) for application in future periods:

International Accounting Standards (IAS / IFRS)	*Effective for annual periods beginning on or after:*
IFRS 7 – Financial Instruments – Disclosures – Offsetting Financial Assets and Liabilities (Amendment)	January 1, 2013
IFRS 9 – Financial Instruments	January 1, 2015
IFRS 10 – Consolidated Financial Statements	January 1, 2013
IFRS 11 – Joint Arrangements	January 1, 2013
IFRS 12 – Disclosure of Interests in Other Entities	January 1, 2013

IFRS 13 – Fair Value Measurement	January 1, 2013
IAS 19 – Employee Benefits (Amendment)	January 1, 2013
IAS 28 – Investments in Associates and Joint Ventures (Amendment)	January 1, 2013
IAS 32 – Financial Instruments: Presentation	January 1, 2014

IFRS 7 Financial Instruments – Disclosures – Offsetting Financial Assets and Financial Liabilities was amended to require additional disclosure when an entity has the right to offset financial assets and financial liabilities and has presented the net amount in the statement of financial position. The Company does not expect this amendment to have a material impact on the financial statements.

IFRS 9 – Financial Instruments replaces IAS 39 – Financial Instruments: Recognition and Measurement, and eliminates the existing categories of financial assets and requires financial assets to be measured as either amortized cost or fair value. Gains and losses on re-measurement of financial assets at fair value will be recognized in profit or loss, except for an investment in an equity instrument which is not held-for-trading. Changes in fair value attributable to changes in credit risk of financial liabilities measured under the fair value option will be recognized in OCI with the remainder of the change recognized in profit or loss unless an accounting mismatch in profit or loss occurs at which time the entire change in fair value will be recognized in profit or loss. Derivative liabilities that are linked to and must be settled by delivery of an unquoted equity instrument must be measured at fair value. The Company does not expect the standard to have a material impact on the financial statements.

IFRS 10 – Consolidated Financial Statements (IFRS 10) replaces IAS 27 – Consolidated and Separate Financial Statements, and Standing Interpretations Committee (SIC) - 12 – Consolidation – Special Purpose Entities, and provides a single model to be applied in the control analysis for all investees, including entities that currently are special purpose entities in the scope of SIC 12. The Company does not expect this standard to have a material impact on the financial statements.

IFRS 11 – Joint Arrangements (IFRS 11) replaces IAS 31 – Interests in Joint Ventures, and SIC 13 - Jointly Controlled Entities - Non-Monetary Contributions by Vendors. IFRS 11 draws a distinction between joint operations and joint ventures. Entities which previously accounted for joint ventures using proportionate consolidation will generally be required to account for such ventures using the equity method. The Company does not expect the standard to have any impact on the treatment of its joint arrangements.

IFRS 12 – Disclosure of Interest in Other Entities (IFRS 12) contains the disclosure requirements for entities that have interests in subsidiaries, joint arrangements, associates and/or unconsolidated structured entities. When applied, it is expected that IFRS 12 will increase the current level of disclosure of the Company’s interest in other entities.

IFRS 13 – Fair Value Measurement replaces the fair value measurement guidance contained in individual IFRS with a single source of fair value measurement guidance. It defines fair value, establishes a framework for measuring fair value and sets out disclosure requirements. The Company does not expect the standard to have a material impact on the financial statements.

IAS 19 – Employee Benefits was amended and introduces changes related to: (a) eliminating the option to defer the recognition of actuarial gains and losses, known as the corridor method, (b) requiring a new method of calculating finance costs on defined benefit plans where a single discount rate is applied to the net pension assets or obligations, and (c) enhancing the disclosure requirements to provide better information about the characteristics of defined benefit plans and the risks that entities are exposed to through participation in these plans. When applied, it is expected that $13 million in previously unrecognized net actuarial losses will be recognized in OCI.

IAS 28 – Investments in Associates and Joint Ventures was amended to conform with IFRS 10 and IFRS 11 accounting standards. The amendments apply to the measurement of a retained stake in an investment where significant influence is succeeded by joint control, and to the measurement of a retained stake in an investment, a portion of which has been classified as held for sale. The Company does not expect these amendments to have any impact on the financial statements.

IAS 32 – Financial Instruments: Presentation provides additional guidance on the application of offsetting criteria. The Company does not expect the standard to have a material impact on the financial statements.

4. Use of judgments and estimates

The preparation of the Company's consolidated financial statements in accordance with IFRS requires management to make judgments in the application of accounting policies, and estimates and assumptions that affect the reported amounts of income, expenses, assets and liabilities as well as the disclosure of contingent assets and liabilities at the date of the consolidated financial statements.

(a) Judgments

Management applied judgment in determining whether the acquisition of Arizona-American Water Company (Water Arizona) and New Mexico-American Water Company, Inc. (Water New Mexico) as described in note 5, constituted a business combination or the purchase of a group of assets.

Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements are included in notes:

Note 3(b) – Business combinations and goodwill
Note 3(c) – Revenue recognition
Note 3(h) – Investment in Capital Power

(b) Estimates

Significant accounting estimates were made in determining the fair value of identifiable assets acquired and liabilities assumed in connection with the Water Arizona and Water New Mexico acquisition including discount rates, future income and cash flows, replacement costs, useful lives, residual values and weighted average cost of capital and the provision for refundable contributions. The fair values were determined using generally accepted methods, as described in note 5, and the assistance of a third party valuation expert.

The Company reviews its estimates and assumptions on an ongoing basis and uses the most current information available and exercises careful judgment in making these estimates and assumptions. Adjustments to previous estimates, which may be material, will be recorded in the period they become known. Actual results may differ from these estimates.

Assumptions and uncertainties that have a significant risk of resulting in a material adjustment within the next financial year include:

Revenues

By regulation, electricity wire service providers in Alberta have four months (2011 – four months) to submit the final electricity load settlement data 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.

Fair value measurement

For certain accounting measures such as determining asset impairments, purchase price allocations for business combinations, recording financial assets and liabilities, recording certain non-financial assets 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. Financial instruments that are not classified as loans and receivables are recorded at fair value, which may require the use of estimated future prices.

Depreciation and amortization

Depreciation and amortization is an estimate to allocate the cost of an asset less its estimated residual value over its estimated useful life on a systematic and rational basis. Estimating the appropriate useful lives of each part of an asset requires significant judgment and is generally based on estimates of common life characteristics of common assets. The estimated useful lives used are provided in notes 3(i) and 3(j). Estimates are reviewed on an annual basis and updated on a prospective basis.

Deferred taxes

Significant estimation and judgment is required in determining the provision for income taxes. Recognition of deferred tax assets in respect of deductible temporary differences and unused tax losses and credits is based on management's estimation of future taxable profit against which the deductible temporary differences and unused tax losses and credits can be utilized. The actual utilization of these deductible temporary differences and unused tax losses and credits may vary materially from the amounts estimated.

5. Acquisition of Water Arizona and Water New Mexico

On January 31, 2012, the Company completed the acquisition of 100% of the stock of Arizona-American Water Company (renamed EPCOR Water Arizona Inc.) and New Mexico-American Water Company, Inc. (renamed EPCOR Water New Mexico Inc.) from American Water Works Company, Inc. for cash consideration of $460 million (US$459 million) and the assumption of $9 million (US$9 million) in long-term debt. Water Arizona and Water New Mexico are public utility companies engaged principally in the purchase, treatment, distribution and sale of water to approximately 126,000 customers in ten water utility districts and wastewater treatment and related services to approximately 52,000 customers in five wastewater utility districts in the states of Arizona and New Mexico. This investment provides the Company with a strong hub in the Southwestern U.S., consistent with the Company's strategic plan for expansion.

Significant judgment was applied in the determination of the fair value of the assets and liabilities acquired, the allocation of the purchase price to those assets and liabilities, and the determination of goodwill. The fair value assessment was supported by a third party valuation. The valuation employed three standard valuation methodologies. Discounted cash flows were used to arrive at enterprise values, using a discount rate of 7% based on prevailing interest rates and the capital structures of the acquired businesses. Other key assumptions were future growth rates and asset terminal values. Depreciated replacement cost techniques were used to estimate the fair values of the non-financial assets acquired. Market comparators were used to determine other financial assets and liabilities. The allocation of the purchase price was determined from the valuation, and where necessary by allocation to assets and liabilities based on relative fair values. Goodwill was estimated based on the applicable incremental benefits of the acquisition, including expected growth in the underlying rate base and the assembled workforce that came with the acquired companies. A 1% increase in the discount rate would result in a reduction of the estimated fair value and increase in the amount of goodwill of $69 million.

The purchase price was allocated to the assets acquired and liabilities assumed based on their estimated fair values in Canadian dollars as follows:

Trade and other receivables	$	11
Intangible assets		94
Goodwill		25
Property, plant and equipment		515
Trade and other payables		(5)
Loans and borrowings		(9)
Deferred revenue		(137)
Provisions (note 3(m))		(33)
Other non-current liabilities		(1)
	$	460

The carrying amount of the acquired trade and other receivables and payables approximate the fair value due to their short-term nature.

The $25 million of goodwill arising from the acquisition consists of the value of an assembled skilled workforce, the expectation of future cash flows and rate recoveries, and the benefits to the Company's growth strategies and future synergies which may result from the Company's expanded operations in the U.S.

The loans and borrowings were repaid in February 2012.

The current amount of provisions for estimated refundable contributions is $3 million.

In October 2012, under the terms of the agreement to acquire Water Arizona and Water New Mexico, the Company exercised its option to file jointly with the vendor a U.S. Internal Revenue Service tax election to treat the acquisition as an asset purchase for income tax purposes. Among other things, this election permits the goodwill to be deductible for income tax purposes.

Revenues of $117 million and net income of $24 million contributed by Water Arizona and Water New Mexico from the date of acquisition to December 31, 2012 are included in the consolidated income statement. The consolidated income statement would have included estimated revenue of $124 million and estimated net income of $24 million to December 31, 2012 had the Company owned the Water Arizona and Water New Mexico operations from the beginning of 2012.

6. Revenues and other income

		2012		2011
Revenue				
Electricity and water sales	$	1,445	$	1,347
Provision of services		456		416
Finance lease income		14		14
Construction revenues		16		17
		1,931		1,794
Other income				
Interest income on long-term receivable with Capital Power		25		38
Other		3		1
		28		39
	$	1,959	$	1,833

7. Expense analysis

		2012		2011
Included in staff costs and employee benefits expenses				
Post-employment defined contribution plan expense	$	25	$	23
Post-employment defined benefit plan expense		2		5
Included in depreciation and amortization				
Depreciation of property, plant and equipment	$	114	$	89
Amortization of intangible assets		15		16
Loss on disposal of assets		3		4
Loss (gain) in decommissioning provision		1		(4)
	$	133	$	105
Included in other administrative expenses				
Operating lease expenses	$	13	$	6

8. Finance expense

	2012	2011
Interest on loans and borrowings	$ 123	$ 119
Capitalized interest (note 21)	(7)	(5)
Interest expense	116	114
Net fair value loss on floating-rate notes	-	1
Net gain on disposal of floating-rate notes	-	(7)
	$ 116	$ 108

9. Impairment of investment in Capital Power

During the fourth quarter, it was determined that the carrying amount of the Company's investment in exchangeable limited partnership units of Capital Power L.P. exceeded the recoverable amount of the investment. The recoverable amount was based on an estimate of the investment's fair value less costs to sell. Fair value was derived from the price of Capital Power Corporation shares (CPX) at the close of the Toronto Stock Exchange on December 31, 2012, less estimated underwriting fees and selling costs of 4% of the total fair value. As a result, the Company recorded a pre-tax impairment charge of $124 million ($124 million after tax), allocated to the corporate business segment.

10. Income tax expense

	2012	2011
Current income tax expense	$ 5	$ 3
Deferred income tax expense		
Relating to origination and reversal of temporary differences	(40)	(6)
Write-down of deferred tax assets	33	5
	(7)	(1)
Total income tax expense (recovery)	$ (2)	$ 2

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

	2012	2011
Income before taxation	$ 16	$ 146
Income tax at the statutory rate of 25.0% (2011 – 26.5%)	4	39
Increase (decrease) resulting from:		
Income exempt from income taxes at statutory rates	(36)	(39)
Unrecognized deferred tax assets	33	6
Effect of higher tax rate in the U.S.	2	-
Adjustments for income tax relating to prior periods	(5)	-
Adjustment for enacted changes in income tax law and rates and other tax rate differences	-	(3)
Other	-	(1)
Total income tax expense (recovery)	$ (2)	$ 2

The reduction in the applicable statutory income tax rate is a result of the decrease in Canadian federal income tax rates from 16.5% in 2011 to 15.0% in 2012.

11. Cash and cash equivalents

	2012	2011
Bank balances	$ 137	$ 102
Short-term investments	95	214
	$ 232	$ 316

Restricted balances

Under certain agreements between the Company and the Natural Gas Exchange (NGX) for the purchase of electricity derivative financial instruments, the Company established separate bank accounts through which the settlement of the electricity derivative financial contracts are processed in conjunction with letters of credit as collateral. As security for the payment and performance of its obligations, the Company assigned a first ranking security interest on the balance of these accounts to the NGX. The Company's use of this cash is restricted to these purposes. At December 31, 2012, $14 million (2011 – $2 million) was held in these bank accounts.

In accordance with the terms of a U.S. subsidiary's long-term debt agreement, the Company is required to maintain amounts on deposit in a trust account for payment of principal and interest. The funds in this account will be maintained until such time that the terms of the financing agreement are fully satisfied. The balance in this account at December 31, 2012 was $1 million (2011 – $1 million).

12. Trade and other receivables

	2012	2011
Trade receivables	$ 222	$ 213
Accrued revenues[1]	115	123
Gross accounts receivable	337	336
Allowance for doubtful accounts	(4)	(4)
Net accounts receivable	333	332
Prepaid expenses	2	3
Income tax recoverable	-	5
	335	340
Current portion of finance lease receivables (note 15)	3	3
Current portion of long-term receivables (note 16)	21	29
	$ 359	$ 372

[1] A $5 increase in wholesale electricity prices will increase the estimated unbilled accrued revenue by $3 million (2011 – $4 million).

Details of the aging of accounts receivable and analysis of the changes in the allowance for doubtful accounts are provided in note 33.

13. Inventories

During the year ended December 31, 2012, $29 million (2011 – $26 million) was expensed to other raw materials and operating charges.

No inventory write-downs were recognized in the years ended December 31, 2012 or 2011. No reversals of previous write-downs were recorded in the years ended December 31, 2012 or 2011.

At December 31, 2012 or 2011, no inventories were pledged as security for liabilities.

14. Derivatives

Derivative financial instruments are held for the purpose of electricity price and foreign exchange risk management.

The derivative instruments assets and liabilities used for risk management purposes as described in note 33 consist of the following:

	December 31, 2012			December 31, 2011		
	Electricity	Foreign exchange	Total	Electricity	Foreign exchange	Total
Derivative instruments assets (liabilities)						
Fair value	$ (4)	$ -	$ (4)	$ (14)	$ 10	$ (4)
Cash paid to counterparty	2	-	2	15	-	15
Net fair value	$ (2)	$ -	$ (2)	$ 1	$ 10	$ 11
Net notional buys						
Megawatt hours of electricity (millions)	0.7	-		0.8	-	
Foreign currency (U.S. dollars)	-	-		-	205	
Range of contract terms (in years)	0.1	-		0.1	0.3	

The fair value of derivative financial instruments reflects changes in the forward electricity prices and foreign exchange rates.

The fair value of electricity derivative financial instruments reflects changes in the electricity prices, net of cash payments to or from the counterparty. During the course of the contract, regular payments are made to or received from the counterparty to settle the fair value of the contracts.

Fair value is determined based on quoted exchange index prices or over-the-counter price quotations by reference to bid or asking price, as appropriate, in active markets. Fair value amounts reflect management's best estimates using external readily observable market data such as future prices, foreign exchange rates and discount rates for time value. It is possible that the assumptions used in establishing fair value amounts will differ from future outcomes and the impact of such variations could be material.

Changes in fair value on electricity derivative financial instruments are recorded in electricity purchases. Changes in fair value of financial foreign exchange derivatives are recorded in foreign exchange gains and losses.

15. Leases

Finance lease receivables

In 2009, the Company acquired potable water and wastewater treatment plant assets for approximately $100 million and agreed to lease the assets back to the vendor for a 20-year term after which the vendor has the option to purchase the assets from the Company for a specified price. As part of the arrangement, the Company also agreed to construct additional water and wastewater treatment plant assets for the vendor and to operate and maintain the original assets acquired and leased back to the vendor and the additional constructed assets over the 20-year lease term.

Approximate future payments to the Company are as follows:

	Minimum lease receivable		Present value of minimum lease receivable	
	2012	2011	2012	2011
Within one year	$ 15	$ 15	$ 3	$ 3
Between one and five years	59	59	18	16
More than five years	174	186	107	111
Less: unearned finance income	(120)	(130)	-	-
	128	130	128	130
Less: current portion[1] (included in trade and other receivables) (note 12)	3	3	3	3
	$ 125	$ 127	$ 125	$ 127

[1] Net of unearned finance income

Operating leases payable

The Company has entered into operating leases for premises.

In 2007, the Company entered into a long-term agreement to lease commercial space in a new office tower in Edmonton primarily for its head office (head office lease). The agreement, which became effective in the fourth quarter of 2011, has an initial lease term of approximately 20 years, expiring on December 31, 2031, and provides for three successive five-year renewal options.

The Company's annual lease commitments, net of annual payments to be paid to the Company by Capital Power and another company under the sub-leases receivable, under the terms of the lease are as follows:

	Minimum lease payable	
	2012	2011
January 1, 2012 through December 31, 2013	$ 7	$ 7
January 1, 2014 through December 31, 2022	6	8
January 1, 2023 through December 31, 2023	7	8
January 1, 2024 through December 31, 2031	8	8

Approximate gross future payments under this and other operating leases payable for premises are as follows:

	Minimum lease payable	
	2012	2011
Within one year	$ 14	$ 14
Between one to five years	56	55
More than five years	180	190
	$ 250	$ 259

Operating lease receivable

The Company has sub-leased a portion of the space under its head office lease to Capital Power under the same terms and conditions as the Company's lease with its landlord. Commencing November 1, 2013, the Company will be sub-leasing a portion of the space under its head office lease to a third party. The term of the sub-lease expires October 31, 2023 with two renewal options of four years each.

Approximate future payments to the Company under the sub-leases receivable are as follows:

	Minimum lease receivable	
	2012	2011
Within one year	$ 4	$ 4
Between one to five years	21	15
More than five years	64	59
	$ 89	$ 78

16. Other financial assets

	2012	2011
Long-term loans receivable from Capital Power	$ 354	$ 379
Loans and other long-term receivables	49	51
Other	1	1
	404	431
Less: current portion (included in trade and other receivables) (note 12)	21	29
	$ 383	$ 402

Long-term loans receivable from Capital Power

On July 9, 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. These loans effectively mirror certain long-term debt obligations of EPCOR. The interest rates on the long-term loans receivable range from 5.8% to 9.0% and the remaining balance will be repaid at various dates out to June 30, 2018 as follows:

	2012	2011
Within one year	$ 14	$ 25
Between one to five years	166	170
More than five years	174	184
	$ 354	$ 379

17. Deferred tax assets / liabilities

Deferred tax assets are attributable to the following:

	2012	2011
Losses carried forward	$ 49	$ 60
Deferred income in partnership	7	-
Intangible assets	8	8
Deferred revenue	59	6
Decommissioning provisions and assets	10	14
Other items	3	3
Tax assets	136	91
Set off by tax liabilities	(84)	(48)
Net tax assets	$ 52	$ 43

Deferred tax liabilities are attributable to the following:

	2012	2011
Investment in partnership	$ 8	$ 29
Deferred income in partnership	3	-
Intangible assets	5	4
Goodwill	1	-
Property, plant and equipment	63	7
Loans and borrowings	-	1
Decommissioning provisions and assets	6	6
Other items	3	2
Tax liabilities	89	49
Set off by tax assets	(84)	(48)
Net tax liabilities	$ 5	$ 1

Deferred net tax assets and liabilities are attributable to the following:

	2012	2011
Losses carried forward	$ 49	$ 60
Investment in partnership	(8)	(29)
Deferred income in partnership	4	-
Intangible assets	3	4
Goodwill	(1)	-
Property, plant and equipment	(63)	(7)
Loans and borrowings	-	(1)
Deferred revenue	59	6
Decommissioning provisions and assets	4	8
Other items	-	1
Net tax assets	$ 47	$ 42

The changes in temporary differences during the years ended December 31, 2012 and 2011 were as follows:

	Balance, beginning of 2012	Recognized in net income	Recognized in other comprehensive income	Recognized through business combinations	Recognized directly in equity	Balance, end of 2012
Losses carried forward	$ 60	$ (11)	$ -	$ -	$ -	$ 49
Investment in partnership	(29)	24	(3)	-	-	(8)
Deferred income in partnership	-	4	-	-	-	4
Intangible assets	4	(1)	-	-	-	3
Goodwill	-	(1)	-	-	-	(1)
Property, plant and equipment	(7)	(3)	-	(53)	-	(63)
Loans and borrowings	(1)	-	1	-	-	-
Deferred revenue	6	-	-	53	-	59
Decommissioning provisions and assets	8	(4)	-	-	-	4
Other items	1	(1)	-	-	-	-
	$ 42	$ 7	$ (2)	$ -	$ -	$ 47

	Balance, beginning of 2011	Recognized in net income	Recognized in other comprehensive income	Recognized directly in equity	Balance, end of 2011
Losses carried forward	$ 68	$ (8)	$ -	$ -	$ 60
Investment in partnership	(31)	2	-	-	(29)
Deferred income in partnership	(7)	7	-	-	-
Intangible assets	3	1	-	-	4
Property, plant and equipment	(2)	(5)	-	-	(7)
Loans and borrowings	(1)	-	-	-	(1)
Deferred revenue	1	5	-	-	6
Decommissioning provisions and assets	8	-	-	-	8
Other items	2	(1)	-	-	1
	$ 41	$ 1	$ -	$ -	$ 42

There were no reclassifications from equity to net income during the year (2011 – nil).

The Company has the following deductible temporary differences for which no deferred tax assets have been recognized:

	2012	2011
Non-capital losses	$ 152	$ 214
Capital losses	282	257
Other deductible temporary differences	105	15

The non-capital losses expire between the years 2013 and 2032.

Deferred tax assets have been recognized to the extent that it is probable that taxable income will be available against which the deductible temporary difference can be utilized. The Company has recognized deferred tax assets in the amount of $47 million (2011 – $38 million) the utilization of which is dependent on future taxable profits in excess of the profits arising from the reversal of existing taxable temporary differences. The recognition of these deferred tax assets is based on taxable income forecasts that incorporate existing circumstances that will result in positive taxable income against which non-capital loss carry-forwards can be utilized as well as management's intention to implement specific income tax planning strategies that will allow for the offset of remaining deductible temporary differences against future earnings of taxable entities within the consolidated group.

18. Investment in Capital Power

At December 31, 2012, the Company owned 28.4 million (2011 – 38.2 million) exchangeable limited partnership units of Capital Power L.P. (exchangeable for common shares of Capital Power Corporation on a one-for-one basis), representing a 29% (2011 – 39%) economic interest in Capital Power. In April 2012, EPCOR exchanged 9,775,000 limited partnership units for an equal number of shares of Capital Power which were immediately sold at an offering price of $23.55 per share for aggregate gross proceeds of $230 million. The Company recorded a $36 million non-cash loss on the sale. The Company's economic interest in Capital Power decreases when it sells a portion of its investment in Capital Power and when Capital Power Corporation issues more common shares, diluting EPCOR's economic interest in Capital Power.

As described in note 3(h), EPCOR does not control Capital Power. The investment in Capital Power represents an investment subject to significant influence and is accounted for using the equity method from the effective date of the sale of the power generation business by EPCOR in early July 2009. The investment was initially recorded at the initial 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 subsequently increases by the Company's equity share of earnings of Capital Power and the Company's equity share of Capital Power's other comprehensive income, and decreases by the limited partnership distributions paid by Capital Power, the Company's equity share of Capital Power's other comprehensive loss, subsequent disposals of portions of the Company's investment and impairment adjustments.

Capital Power Corporation is listed on the Toronto Stock Exchange under the symbol CPX. The quoted market price of the common shares of Capital Power Corporation at December 31, 2012 was $22.73 per common share (December 31, 2011 – $25.12 per common share).

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

	2012	2011
Balance, beginning of year	$ 987	$ 1,192
Equity share of net income	41	90
Equity share of other comprehensive income (loss)	14	(5)
Distributions declared	(39)	(57)
Sale of a portion of the investment and dilutions	(258)	(233)
Impairment (note 9)	(124)	-
Balance, end of year	$ 621	$ 987

Summarized financial information of Capital Power L.P.:

	2012	2011
Statements of Financial Position		
Current assets	$ 515	$ 395
Non-current assets	4,648	4,402
Current liabilities	(363)	(394)
Non-current liabilities	(2,183)	(1,823)
Non-controlling interests	(94)	(97)
Net assets	$ 2,523	$ 2,483

	2012	2011
Consolidated Income Statements		
Revenue and other income	$ 1,319	$ 1,763
Net income attributable to partners	120	213

19. Intangible assets

	Goodwill (note 20)	Customer rights	Other rights	CCN	Software	Total
Cost						
Balance, beginning of 2012	$ 11	$ 51	$ 7	$ -	$ 162	$ 231
Additions through acquisition	-	-	-	-	10	10
Additions through business combination	25	-	31	63	-	119
Internally generated additions	-	-	-	-	5	5
Disposals and retirements	-	-	-	-	(14)	(14)
Foreign currency translation adjustments	-	-	-	(1)	-	(1)
Balance, end of 2012	36	51	38	62	163	350
Accumulated amortization						
Balance, beginning of 2012	-	27	1	-	99	127
Amortization	-	3	1	-	11	15
Disposals and retirements	-	-	-	-	(14)	(14)
Balance, end of 2012	-	30	2	-	96	128
Net book value, end of 2012	$ 36	$ 21	$ 36	$ 62	$ 67	$ 222

	Goodwill (note 20)	Customer rights	Other rights	CCN	Software	Total
Cost						
Balance, beginning of 2011	$ 2	$ 70	$ 3	$ -	$ 167	$ 242
Additions through acquisition	-	-	-	-	1	1
Additions through business combination	9	-	3	-	-	12
Internally generated additions	-	-	1	-	6	7
Disposals and retirements	-	(19)	-	-	(12)	(31)
Balance, end of 2011	11	51	7	-	162	231
Accumulated amortization						
Balance, beginning of 2011	-	44	1	-	97	142
Amortization	-	2	-	-	14	16
Disposals and retirements	-	(19)	-	-	(12)	(31)
Balance, end of 2011	-	27	1	-	99	127
Net book value, end of 2011	$ 11	$ 24	$ 6	$ -	$ 63	$ 104

There are no security charges over the Company's intangible assets. Included in customer rights are the Company’s customer rights to operate in the FortisAlberta service territory which expire on December 31, 2020.

20. Goodwill

	2012	2011
Cost		
Balance, beginning of year	$ 11	$ 2
Additions through business combinations	25	9
Balance, end of year	36	11
Accumulated impairment		
Balance, beginning of year	-	-
Impairments	-	-
Balance, end of year	-	-
Net book value, end of year	$ 36	$ 11

For purposes of impairment testing, goodwill acquired through business combinations has been allocated to cash-generating units as follows:

	2012	2011
Cash generating unit:		
Water segment – French Creek	$ 1	$ 1
Water segment – White Rock	1	1
Water segment – Chaparral	9	9
Water segment – Water Arizona	22	-
Water segment – Water New Mexico	3	-
	$ 36	$ 11

The most recent reviews of goodwill were performed in the fourth quarter for each cash generating unit. Management reviewed conditions since the last review was performed and determined that no circumstances occurred since then to require a revision to the assumptions used in the value-in-use calculations.

The recoverable amount of the cash generating units was determined based on a value-in-use calculation using cash flow projections from financial budgets approved by senior management covering a twenty year period. The projections were based on cash flow projections for the most recent rate applications, which covered periods up to 3 years, with the projections for the balance of the twenty-year period extrapolated using growth rates between 2.1% and 2.6% (2011 – between 2.0% and 2.6%) that are in line with the long-term average growth rate for the industry. The pre-tax discount rates applied to cash flow projections are as follows:

	2012	2011
Cash generating unit:		
Water segment – French Creek	8.18%	8.16%
Water segment – White Rock	7.82%	7.82%
Water segment – Chaparral	7.58%	7.50%
Water segment – Water Arizona	6.97%	N/A
Water segment – Water New Mexico	7.00%	N/A

Key assumptions used in value in use calculations

The future cash flows of the underlying businesses are relatively stable, since they relate to ongoing water supply in a rate regulated environment. As the cash generating units operate under a rate regulated environment, revenues are set by the regulators to cover operating costs and to earn a return on the rate base, which is set at the regulator's approved weighted average cost of capital for the underlying utility.

The calculation of value in use for the cash generating units is most sensitive to the following assumptions:

Discount rates

The discount rates used were estimated based on the weighted average cost of capital for the cash generating unit, which is the approved rate of return on capital allowed by the regulators. This rate was further adjusted to reflect the market assessment of any risk specific to the cash generating unit for which future estimates of cash flows have not been adjusted.

Timing of future rate increases

Revenue growth is forecast to continue at the same rate as operating costs. If future rate filings are delayed, rate increases and increased cash flows from revenues would be affected.

Sensitivity to changes in assumptions

Assumptions have been tested using reasonably possible alternative scenarios. For all scenarios considered, the recoverable value remained above the carrying amount of the cash generating unit.

21. Property, plant and equipment

	Construction work in progress	Land	Water treatment & distribution	Electricity transmission & distribution	Retail systems & equipment	Corporate information systems & other	Total
Cost							
Balance, beginning of 2012	$ 96	$ 30	$ 2,015	$ 1,354	$ 14	$ 78	$3,587
Additions	117	-	115	136	1	4	373
Additions through business combinations	8	6	501	-	-	-	515
Disposals and retirements	-	(1)	(8)	(6)	(8)	-	(23)
Transfers into service	(53)	-	24	29	-	-	-
Foreign currency valuation adjustments	-	-	(5)	-	-	-	(5)
Balance, end of 2012	168	35	2,642	1,513	7	82	4,447
Accumulated Depreciation							
Balance, beginning of 2012	-	-	496	400	6	27	929
Depreciation	-	-	62	42	1	9	114
Disposals and retirements	-	-	(5)	(4)	(4)	-	(13)
Balance, end of 2012	-	-	553	438	3	36	1,030
Net book value, end of 2012	$ 168	$ 35	$ 2,089	$ 1,075	$ 4	$ 46	$3,417

	Construction work in progress	Land	Water treatment & distribution	Electricity transmission & distribution	Retail systems & equipment	Corporate information systems & other	Total
Cost							
Balance, beginning of 2011	$ 71	$ 30	$ 1,867	$ 1,209	$ 15	$ 79	$3,271
Additions	63	-	98	129	1	36	327
Additions through business combinations	1	-	38	-	-	-	39
Disposals and retirements	-	-	(6)	(5)	(2)	(39)	(52)
Transfers into service	(39)	-	16	21	-	2	-
Foreign currency valuation adjustments	-	-	2	-	-	-	2
Balance, end of 2011	96	30	2,015	1,354	14	78	3,587
Accumulated Depreciation							
Balance, beginning of 2011	-	-	461	365	7	53	886
Depreciation	-	-	39	38	1	10	88
Disposals and retirements	-	-	(5)	(3)	(2)	(36)	(46)
Other changes and movements	-	-	1	-	-	-	1
Balance, end of 2011	-	-	496	400	6	27	929
Net book value, end of 2011	$ 96	$ 30	$ 1,519	$ 954	$ 8	$ 51	$2,658

Borrowing costs capitalized during the year ended December 31, 2012 were $7 million (2011 – $5 million) (note 8). The weighted average rates used to determine the borrowing costs eligible for capitalization ranged from 4.30% to 7.91% (2011 – 5.19% to 7.05%).

Restrictions on assets

Assets with a net book value of $41 million (2011 – $41 million) have been pledged as security against certain subsidiary bonds with a net carrying amount of $5 million (2011 – $6 million) (note 24).

22. Investment in Heartland Transmission Project

EPCOR owns a 50% interest in the Heartland electricity transmission line as described in note 3(t). The financial statements of the joint venture have been incorporated into these consolidated financial statements based on EPCOR's relative share of the joint venture's assets, liabilities, revenue and expenses with items of a similar nature on a line-by-line basis. Since the project is under construction at December 31, 2012, project revenues were nil (2011 – nil) and project operating expenses were nil (2011 – nil).

The summarized financial information of the Heartland Transmission Project joint venture is detailed as follows:

	2012	2011
Statements of Financial Position		
Intangible assets	$ 2	$ 2
Property, plant and equipment	204	81
Net assets	$ 206	$ 83

The joint venture's remaining capital commitments are $211 million (2011 – $259 million). The joint venture's total expected cost is $417 million (2011 – $400 million).

23. Trade and other payables

	2012	2011
Trade payables	$ 204	$ 151
Accrued liabilities	40	50
Accrued interest	29	28
Due to related parties	13	22
Due to employees	15	13
Income tax payable	2	-
	$ 303	$ 264

24. Loans and borrowings

	Effective interest rate	2012	2011
Obligation to the City, net of sinking fund			
Due in 1-5 years at 8.76% (2011 - 8.91%)	10.25%	$ 4	$ 11
Due in 6-10 years at 8.14% (2011 - 8.50%)	9.96%	58	45
Due in 11-15 years at 6.18% (2011 - 7.01%)	6.18%	1	22
Due in 16-25 years at 5.20% (2011 - 5.21%)	5.36%	88	94
		151	172
Public debentures			
At 6.75%, due in 2016	6.94%	130	130
At 5.80%, due in 2018	6.02%	400	400
At 6.80%, due in 2029	7.05%	150	150
At 5.65%, due in 2035	5.88%	200	200
At 6.65%, due in 2038	6.83%	200	200
At 5.75%, due in 2039	5.88%	200	200
At 4.55%, due in 2042	4.65%	300	-
		1,731	1,452
Private debt notes			
Bonds at 3.74%, due in 2021	3.80%	137	140
Bonds at 5.40%, due in 2022	5.55%	4	5
Bonds at 5.30%, due in 2022	5.44%	1	1
Bonds at 5.00%, due in 2041	5.08%	111	114
		1,984	1,712
Other borrowings			
Deferred debt issue costs		(14)	(13)
		1,970	1,699
Less: current portion		14	17
		$ 1,956	$ 1,682

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. A portion of the 8.14% debentures, maturing in the year 2018 and totaling $40 million, rank as subordinated debt. In the event of default on 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 sinking fund requirements, the payment obligation ceases on maturity of the debenture.

In 2009, the City transferred the Gold Bar wastewater treatment plant (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 5.10%.

Public debentures

The public 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.

Commercial paper and bankers' acceptances

Bank lines of credit are unsecured and are available to the Company up to an amount of $945 million, comprised of committed amounts of $900 million and uncommitted amounts of $45 million as described in note 33. Letters of credit totaling $139 million (2011 – $272 million) have been issued under these facilities as described in note 36. Amounts borrowed, and letters of credit issued, if any, under these facilities which are not payable within one year are classified as non-current loans and borrowings.

The Company’s commercial paper program has an authorized capacity of $500 million. The commercial paper issuance limit of $225 million was removed from the committed credit facilities effective January 31, 2012. The Company had no commercial paper outstanding at December 31, 2012 (2011 – nil).

Private debt notes

The private debt notes due in 2021 and 2041 were issued in U.S. dollars, 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 private debt notes are redeemable by the Company prior to maturity at the greater of par and a price specified under the terms of the private debt notes.

The private debt notes due in 2022 were issued in U.S. dollars and are secured direct obligations of the Company. Assets with a net book value of $41 million (2011 – $41 million) have been pledged as security. The notes are redeemable prior to maturity at a price specified under the terms of the private debt notes.

25. Deferred revenue

	2012	2011
Balance, beginning of year	$ 602	$ 544
Contributions received	45	57
Acquired on business combination	137	12
Revenue recognized	(20)	(12)
Foreign currency valuation adjustments	(2)	1
	762	602
Less: current portion	21	16
Balance, end of year	$ 741	$ 586

26. Provisions

	2012	2011
Contributions from customers and developers	$ 31	$ 5
Decommissioning	1	4
Employee benefits	67	43
	99	52
Less: current portion	29	18
	$ 70	$ 34

Contributions from customers and developers

	2012	2011
Balance, beginning of year	$ 5	$ -
Contributions received	4	5
Acquired on business combination	25	-
Contributions refunded	(3)	-
Balance, end of year	$ 31	$ 5

Decommissioning

	2012	2011
Balance, beginning of year	$ 4	$ 11
Arising during the year	-	(3)
Utilized	(3)	(4)
Disposal	-	-
Balance, end of year	$ 1	$ 4

The carrying amount of the decommissioning provision has not been discounted as the obligation is expected to be settled in 2013.

Employee benefits

	2012	2011
Other short-term employee benefit obligation	$ 18	$ 14
Post-employment benefit obligation	24	15
Other long-term employee benefit obligation	25	14
	$ 67	$ 43

Other long-term employee benefits

Other long-term employee benefits consist mainly of obligations for benefits provided to employees on long-term disability leaves.

Post-employment benefits

Total cash payments for pension benefits for the year ended December 31, 2012, consisting of cash contributed by the Company to the LAPP, other defined contribution and benefit plans, and cash payments directly to beneficiaries for their unfunded pension plan, were $27 million (2011 – $28 million). Total contributions expected to be paid in 2013 to the LAPP, other defined contribution and benefit plans, and cash payments directly to beneficiaries for their unfunded pension plan are $29 million (2011 – $27 million).

27. Other liabilities

	2012	2011
Gold Bar transfer fee payable	$ 17	$ 29
Customer deposits	20	21
Leasehold inducements	12	13
	49	63
Less: current portion	31	34
	$ 18	$ 29

28. Share capital

Authorized shares

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

Issued shares

Three common shares for nominal value to the City.

29. Accumulated other comprehensive income

Cash flow hedges

This comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that had not yet occurred prior to the disposal of the power generation business in 2009. On any disposition of the Company's investment in Capital Power, the Company will recognize a portion of these losses in net income in proportion to the remaining interest in Capital Power sold.

Available-for-sale financial assets

This comprises the cumulative net change in the fair value of the Company's beneficial interest in the sinking fund, until the investment is derecognized or impaired.

Cumulative translation accounts

The cumulative translation accounts for foreign operations represent the cumulative portion of gains and losses on retranslation of foreign operations that have a functional currency other than Canadian dollars. The cumulative deferred gain or loss on the foreign operation is reclassified to income or loss only on disposal of the foreign operation.

Investment in Capital Power

The investment in Capital Power comprises the Company's equity share in other comprehensive income and loss of Capital Power.

30. Change in non-cash working capital

		2012		2011
Trade receivables (note 12)	$	(1)	$	(69)
Prepaid expenses (note 12)		1		-
Income tax recoverable (note 12)		5		(4)
Inventories		(1)		(2)
Trade and other payables (note 23)		39		5
Other current liabilities (note 27)		-		1
	$	43	$	(69)

		2012		2011
Included in specific items on statements of cash flows:				
Finance expense	$	1	$	(3)
Income tax expense		(6)		(10)
Distributions from Capital Power		3		3
Payment of Gold Bar transfer fees		-		(2)
Acquisition of Water Arizona and Water New Mexico		(5)		-
		(7)		(12)
Decrease in working capital resulting from a change in current portion of long-term receivable		7		(1)
Operating activities		64		(85)
Investing activities		(21)		29
	$	43	$	(69)

31. Related party balances and transactions

Compensation of key management personnel

		2012		2011
Short-term employee benefits	$	4	$	3
Post-employment benefits		1		1
Other long-term benefits		2		1
	$	7	$	5

The Company provides utility services to key management personnel as it is the sole provider of certain services. Such services are provided in the normal course of operations and are based on normal commercial rates, as approved by regulation.

Other related party transactions

The Company is 100% owned by the City. The Company provides maintenance, repair and construction services, and customer billing services to the City, and purchases printing services and supplies, mobile equipment services, public works and various other services pursuant to service agreements. Sales between the Company and the City are in the normal course of operations, and are generally based on normal commercial rates, or as agreed to by the parties.

Transactions between EPCOR and its subsidiary companies are eliminated on consolidation.

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

	2012	2011
Consolidated Income Statements		
Revenues (a)	$ 97	$ 90
Other raw materials and operating charges (b)	15	14
Franchise fees and property taxes (c)	79	76
Finance expense (d)	17	25

(a) Included within revenues are electricity and water sales of $3 million (2011 – $2 million), service revenue including the provision of maintenance, repair and construction services of $86 million (2011 – $81 million), and customer billing services of $8 million (2011 – $7 million).

(b) Includes certain costs of printing services and supplies, mobile equipment services, public works and various other services pursuant to service agreements.

(c) Comprised of franchise fees of $50 million (2011 – $49 million) at 0.66 cents per kilowatt hour of electric distribution capacity (2011 – 0.66 cents per kilowatt hour), franchise fees of $16 million at 8% (2011 – $15 million at 8%) of qualifying revenues of water services and Gold Bar, and property taxes of $13 million (2011 – $12 million) on properties owned within the City municipal boundaries.

(d) Comprised of interest expense on the obligation to the City at interest rates ranging from 5.20% to 9.00% (2011 – 5.21% to 9.01%).

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

	2012	2011
Consolidated Statements of Financial Position		
Trade and other receivables	$ 30	$ 23
Property, plant and equipment (e)	2	3
Trade and other payables (f)	11	20
Loans and borrowings (note 24)	151	172
Deferred revenue (g)	26	20
Other liabilities (h) (note 27)	17	29
Equity attributable to the Owner of the Company	24	24

(e) Costs of capital construction for water distribution mains and infrastructure.

(f) Includes $2 million (2011 – $2 million) for drainage and construction services provided by the City.

(g) Capital contributions received for capital projects and rebates relating to maintenance, repair and construction services.

(h) Relates to a transfer fee payable to the City for Gold Bar of which $10 million (2011 – $12 million) is the current portion and $7 million (2011 – $17 million) is the non-current portion.

The Company has a 29% interest in Capital Power. The Company provides distribution and transmission services to Capital Power and up to June 30, 2011, Capital Power provided electricity under contracts to the Company. Transactions are in the normal course of operations and are based on normal commercial rates, as approved by regulation.

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

	2012	2011
Consolidated Income Statements		
Revenues (i)	$ 25	$ 29
Other income (j)	25	39
Electricity purchases	-	230
Other raw materials and operating charges (k)	8	7
Other administrative expenses (l)	(6)	-
Equity share of income of Capital Power (note 18)	41	90
Other Comprehensive Income		
Equity other comprehensive income (loss) (note 18)	14	(5)

(i) Relates to electricity distribution and transmission services provided to Capital Power by EPCOR.

(j) Relates to financing revenue on long-term receivable.

(k) Relates to utility bills and charges for provision of transitional services by Capital Power to EPCOR under services agreements.

(l) Relates to the provision of services by EPCOR to Capital Power under services agreements.

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

	2012	2011
Consolidated Statements of Financial Position		
Trade and other receivables (m)	$ 18	$ 22
Other financial assets (note 16)	354	379
Trade and other payables	2	2
Deferred revenue (n)	(7)	(7)

(m) Includes $6 million (2011 – $6 million) relating to the accrued interest on the long-term receivable from Capital Power (note 16).

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

32. Fair values of financial instruments

The classification, carrying amounts and fair values of the Company's other financial instruments at December 31, 2012 and 2011 is summarized as follows:

		2012		2011	
	Classification	Carrying amount	Fair value	Carrying amount	Fair value
Cash and cash equivalents (note 11)	Fair value through profit or loss	$ 232	$ 232	$ 316	$ 316
Trade and other receivables (note 12)	Loans and receivables	335	335	340	340
Derivatives (note 14)	Fair value through profit or loss	(2)	(2)	11	11
Finance lease receivables (note 12 and 15)	Loans and receivables	128	146	130	145
Other financial assets (notes 12 and 16)	Loans and receivables	404	447	431	486
Trade and other payables (note 23)	Other liabilities	303	303	264	264
Loans and borrowings (note 24)					
Debentures and borrowings	Other liabilities	2,128	2,561	1,943	2,336
Beneficial interest in sinking fund	Available for sale	(158)	(158)	(244)	(244)
Other liabilities (note 27)					
Customer deposits	Other liabilities	20	20	21	21
Gold Bar transfer fee payable	Other liabilities	17	17	29	29

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 instruments either directly or indirectly. A Level 3 valuation for the assets and liabilities are not based on observable market data.

Cash and cash equivalents

The fair value of cash and cash equivalents is determined by unadjusted quoted prices from active markets. Cash and cash equivalents are classified in Level 1.

Trade and other receivables

Trade and other receivables are initially measured at cost and after initial recognition, are measured at amortized cost. Due to the short-term nature of these assets, fair value is not materially different from carrying amount. Trade and other receivables are classified in Level 3.

Derivatives

Fair value is determined based on exchange index prices in active markets. Fair value amounts reflect management's best estimates using external readily observable market data such as future prices. It is possible that the assumptions used in establishing fair value amounts will differ from future outcomes and the impact of such variations could be

material. Derivative financial assets are classified in Level 1.

Finance lease receivables

The fair values of the Company's finance lease receivables are based on the estimated interest rates implicit in comparable lease arrangements or loans plus an estimated credit spread based on the counterparty risk at December 31, 2012 and December 31, 2011. Finance lease receivables are classified in Level 2.

Loans and other long-term receivables

The fair value of the Company's unsecured long-term receivable from Capital Power is based on a current yield for the Company's receivable at December 31, 2012 and December 31, 2011. 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. The long-term receivable from Capital Power is classified in Level 2.

The fair values of the Company's other long-term loans and receivables are based on the estimated interest rates implicit in comparable loan arrangements plus an estimated credit spread based on the counterparty risks at December 31, 2012 and December 31, 2011. Other long-term loans and receivables are classified in Level 2.

Trade and other payables

Trade and other payables are initially measured at cost and after initial recognition, are measured at amortized cost. Due to the short-term nature of these liabilities, fair value is not materially different from carrying amount. Trade and other payables are classified in Level 3.

Loans and borrowings

Short-term debt is measured at amortized cost and its fair value is not materially different from its carrying amount due to its short-term nature. Short-term debt is classified in Level 3.

The fair value of the Company's long-term loans and borrowings is based on determining a current yield for the Company's debt at December 31, 2012 and December 31, 2011. This yield is based on an estimated credit spread for the Company over the yields of long-term Government of Canada bonds for Canadian dollar loans and U.S. Treasury bonds for U.S. dollar loans 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. The Company's long-term loans and borrowings (including the current portion) include 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 a related party balance and has been recorded at fair value as it has been classified as an available-for-sale financial asset. The fair value of the beneficial interest in the sinking fund is based on quoted market values as determined by the City at or near the reporting date and is classified in Level 1. Long-term loans and borrowings are classified in Level 2.

Other liabilities

Customer deposits and Gold Bar transfer fee payable are initially measured at cost and after initial recognition, are measured at amortized cost. Due to the short-term nature of customer deposits and Gold Bar transfer fee payable fair values are not materially different from carrying amount. Customer deposits and Gold Bar transfer fee payable are classified in Level 3.

33. 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. EPCOR's 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. The back-to-back debt obligations may be called by EPCOR for repayment once its ownership interest in Capital Power is below 20%. The repayment must occur within 180 days of notice if the principal balance outstanding is less than $200 million or 365 days of notice if the principal balance outstanding is equal to or greater than $200 million.

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 has no ability to manage these risks directly. 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 input into certain of the operating and strategic decisions made by Capital Power, including risk management. EPCOR can indirectly reduce its exposure to these risks by reducing its interest in Capital Power.

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.

Market risk

Market risk is the risk of loss that results from changes in market factors such as electricity 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 financial instruments such as forward contracts or contracts-for-differences. Such instruments may be used to establish a fixed price for an anticipated transaction denominated in a foreign currency or electricity.

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.

Electricity price and volume risk

EPCOR sells electricity to regulated rate option (RRO) customers under a RRT. The amount of electricity to be procured, the procurement method and electricity selling prices to be charged to these customers is determined by the EPSP under

which the Company directly manages procurement of the electricity for the RRO customers. All electricity for the RRO customers is purchased in real time from the AESO in the spot market. Under the EPSP, the Company uses financial contracts to hedge the RRO requirements and incorporate the price into customer rates for the applicable month. Fixed volumes of electricity are purchased at fixed prices using financial contracts-for-differences up to 45 days in advance of the month in which the electricity (load) is consumed by the RRO customers. The volume of electricity purchased in advance is based on load (usage) forecasts for the consumption month. When consumption varies from forecast consumption patterns, EPCOR is exposed to prevailing market prices because it must either buy electricity if its volumes procured are short of actual load requirements or sell the electricity if its volumes procured are greater than the actual load requirements (long). Exposure to variances in electricity volume can be exacerbated by other events such as unexpected generation plant outages and unusual weather patterns. In January 2013, the Government of Alberta announced that the province will extend the purchasing window from 45 days to 120 days. EPCOR's current EPSP allows a purchase window of 45 days, however, the Company has agreed in principle with its customer representatives to amend its EPSP to include this extension.

Under contracts-for-differences the Company agrees to exchange, with a single creditworthy and adequately secured counterparty, the difference between the AESO electricity spot market price and the fixed contract price for a specified volume of electricity up to 45 days (120 days effective January 2013) in advance of the consumption date, all in accordance with the EPSP. The contracts-for-differences are referenced to the AESO electricity spot price and any movement in the AESO price results in changes in the contract settlement amount. If the risks of the EPSP were to become untenable, EPCOR could test the market and potentially re-contract the procurement risk under an outsourcing arrangement at a certain cost that would likely increase procurement costs and reduce margins.

At December 31, 2012, holding all other variables constant, a $5 per megawatt hour increase / decrease in the forward electricity spot price would increase / decrease net income by approximately $3 million (2011 – $4 million). In preparing the sensitivity analysis, the Company compared average AESO electricity spot prices to the forward index price for the past 24 months. Based on historical fluctuations, the Company estimates that the fair value of the contracts could increase or decrease by up to $19 million (2011 – $25 million) with a corresponding change to net income.

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 subsidiaries.

The Company's Financial Exposure 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 commitments denominated in U.S. dollars. 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 foreign currency 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, 2012 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 also 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. At December 31, 2012 and December 31, 2011 all long-term debt was fixed rate. The Company may also use derivative financial instruments to manage interest rate risk. At December 31, 2012 and December 31, 2011, the Company did not hold any interest rate derivative financial instruments.

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 a 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 is represented by the carrying amount of the following financial assets (liabilities):

	2012	2011
Cash and cash equivalents[1] (note 11)	$ 232	$ 316
Trade and other receivables[2] (note 12)	333	332
Derivatives (note 14)	(2)	11
Finance lease receivables (note 15)	128	130
Loans and other long-term receivables (notes 12 and 16)	404	431
Investment in Capital Power (note 18)	621	987
	$ 1,716	$ 2,207

[1] This table does not take into account collateral held. At December 31, 2012, the Company held cash deposits of $34 million (2011 – $23 million) as security for certain counterparty accounts receivable and derivative contracts. The Company is not permitted to sell or re-pledge this collateral in the absence of default of the counterparties providing the collateral.

[2] The Company's maximum exposures related to trade and other receivables by major credit concentration is comprised of $269 million (2011 – $282 million) related to rate regulated customer balances. At December 31, 2012, the Company held credit enhancements to mitigate credit risk on trade and other receivables in the form of letters of credit of $1 million (2011 – $2 million) and parental guarantees of $23 million (2011 – $16 million).

Credit quality and concentrations

The Company is exposed to credit risk on outstanding trade receivables associated with its water and electricity sales activities and agreements with the AESO and on electricity supply agreements with wholesale and retail customers. The Company is also exposed to credit risk from its cash and cash equivalents, derivative instruments and long-term financing arrangements receivable.

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

At December 31, 2012:

	Investment grade or secured[1,2] %	Unrated %
Trade and other receivables		
Rate regulated customers[3]	-	100%
Distribution and Transmission customers	87%	13%
Water customers	29%	71%
Cash and cash equivalents	100%	-
Loans and other long-term receivables	100%	-

At December 31, 2011:

	Investment grade or secured[1,2] %	Unrated %
Trade and other receivables		
Rate regulated customers[3]	-	100%
Distribution and Transmission customers	83%	17%
Water customers	28%	72%
Cash and cash equivalents	100%	-
Loans and other long-term receivables	100%	-

[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] Certain trade receivables 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.

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

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 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.

Trade and other receivables and allowance for doubtful accounts

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

The aging of trade and other receivables was:

	December 31, 2012		
	Gross trade and other receivables	Allowance for doubtful accounts	Net trade and other receivables
Current[1]	$ 296	$ -	$ 296
Outstanding 31 to 60 days	29	-	29
Outstanding 61 to 90 days	7	2	5
Outstanding more than 90 days	5	2	3
	$ 337	$ 4	$ 333

	December 31, 2011		
	Gross trade and other receivables	Allowance for doubtful accounts	Net trade and other receivables
Current[1]	$ 304	$ -	$ 304
Outstanding 31 to 60 days	18	-	18
Outstanding 61 to 90 days	10	3	7
Outstanding more than 90 days	4	1	3
	$ 336	$ 4	$ 332

[1] Current amounts represent trade and other receivables outstanding up to 30 days. Amounts outstanding for more than 30 days are considered past due.

Bad debt expense of $9 million (2011 – $7 million) recognized in the year 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 trade and other receivables. Allowances and write-offs are determined by each business unit, either by applying specific risk factors to customer groups' aged balances in trade and other receivables or by reviewing material accounts on a case-by-case basis. Reductions in trade and other 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:

	2012	2011
Balance, beginning of year	$ 4	$ 3
Additional allowances created	8	6
Recovery of receivables	1	1
Receivables written off	(9)	(6)
Balance, end of year	$ 4	$ 4

At December 31, 2012, the Company held $20 million (2011 – $21 million) of customer deposits for the purpose of mitigating the credit risk associated with trade and other receivables from residential and business customers.

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 Company's 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 and financings in public or private debt capital markets.

The Company has revolving extendible credit facilities, which are used principally for the purpose of backing the Company's commercial paper program and providing letters of credit, as outlined below:

December 31, 2012	Expiry	Total facilities	Banking commercial paper issued	Letters of credit and other facility draws	Net amounts available
Committed					
Syndicated bank credit facility Tranche A	November 2015	$ 250	$ -	$ -	$ 250
Syndicated bank credit facility[1]	November 2015	400	-	139	261
Syndicated bank credit facility Tranche B	November 2017	250	-	-	250
Total committed		900	-	139	761
Uncommitted					
Bank line of credit	No expiry	25	-	-	25
Bank line of credit	November 2013	20	-	-	20
Total uncommitted		45	-	-	45
		$ 945	$ -	$ 139	$ 806

December 31, 2011	Expiry	Total facilities	Banking commercial paper issued	Letters of credit and other facility draws	Net amounts available
Committed					
Syndicated bank credit facility Tranche A	November 2014	$ 250	$ -	$ -	$ 250
Syndicated bank credit facility Tranche B	November 2016	250	-	203	47
Total committed		500	-	203	297
Uncommitted					
Bank lines of credit	No expiry	120	-	50	70
Bank line of credit	November 2012	20	-	19	1
Total uncommitted		140	-	69	71
		$ 640	$ -	$ 272	$ 368

[1] Restricted to letters of credit.

The Company has credit ratings of BBB+ and A (low), assigned by Standard and Poor's and DBRS Limited, respectively. In January 2012, the Company established an additional $400 million committed syndicated bank credit facility in order to provide an additional source of liquidity. The facility can only be used to provide letters of credit. The extension feature of EPCOR's committed syndicated bank credit facilities give the Company the option each year to re-price and extend the terms of the facilities by one or more years subject to agreement with the lending syndicate.

The Company has a Canadian shelf prospectus under which it may raise up to $1 billion of debt with maturities of not less than one year. In February 2012, the Company issued $300 million, 4.55% medium-term notes due February 2042 under its base shelf prospectus. The notes were priced to yield 4.565%, pay interest semi-annually and rank equally, except as

to the sinking fund and statutory preferred exceptions, with all other unsecured and unsubordinated indebtedness of the Company. The notes were used to pay down commercial paper indebtedness and for general corporate purposes. At December 31, 2012, the available amount remaining under this shelf prospectus was $700 million (2011 – $1 billion). The shelf prospectus expires in January 2014.

The following are the undiscounted cash flow requirements and contractual maturities of the Company's financial liabilities, including interest payments, at December 31, 2012:

	2013	2014	2015	2016	2017	2018 and thereafter	Total contractual cash flows
Financial liabilities							
Trade and other payables[1]	$ 274	$ -	$ -	$ -	$ -	$ -	$ 274
Loans and borrowings	18	14	15	145	15	1,777	1,984
Interest payments on loans and borrowings	122	117	117	112	107	1,379	1,954
Other liabilities	21	1	1	1	1	7	32
Gold Bar transfer fee liability[2]	10	6	1	-	-	-	17
	$ 445	$ 138	$ 134	$ 258	$ 123	$ 3,163	$ 4,261

[1] Excluding accrued interest on loans and borrowings of $29 million.

[2] In 2009, the City transferred Gold Bar to EPCOR. In exchange for the net assets transferred, EPCOR agreed to pay a total transfer fee of $75 million, of which $17 million remains payable.

The following are the undiscounted cash flow requirements and contractual maturities of the Company's financial liabilities, including interest payments, at December 31, 2011:

	2012	2013	2014	2015	2016	2017 and thereafter	Total contractual cash flows
Financial liabilities							
Trade and other payables[1]	$ 236	$ -	$ -	$ -	$ -	$ -	$ 236
Loans and borrowings	25	18	15	15	145	1,494	1,712
Interest payments on loans and borrowings	118	109	104	103	98	1,142	1,674
Other liabilities	21	2	1	1	1	8	34
Gold Bar transfer fee liability	12	10	6	1	-	-	29
	$ 412	$ 139	$ 126	$ 120	$ 244	$ 2,644	$ 3,685

[1] Excluding accrued interest on loans and borrowings of $28 million.

The Company's undiscounted cash flow requirements and contractual maturities in the next twelve months of $445 million are expected to be funded from operating cash flows, partnership distributions from Capital Power L.P., interest and principal payments related to the unsecured long-term receivable from Capital Power, commercial paper issuance and the Company's credit facilities. In addition, the Company may issue medium-term notes or sell a portion of the investment in Capital Power or other assets to fund its obligations or investments. The key factors in determining whether to issue medium-term notes or sell a portion of the investment in Capital Power are the expected interest rates for medium-term notes, the estimated demand by investors for EPCOR debt, the state of debt capital markets generally, the quoted price of Capital Power common shares, potential limits posed by the underlying agreements with Capital Power, the estimated demand by equity investors, and the state of equity capital markets generally,

The Company has long-term loans receivable from Capital Power which effectively match certain of the long-term loans

and borrowings above. The following are the undiscounted maturities of the long-term loans receivable and interest payments from Capital Power at December 31, 2012:

	2013	2014	2015	2016	2017	2018 and thereafter	Total
Long-term loans receivable from Capital Power (note 16)	$ 14	$ 8	$ 9	$ 139	$ 10	$ 174	$ 354
Interest payments on loans receivable from Capital Power	23	22	21	16	11	6	99
	$ 37	$ 30	$ 30	$ 155	$ 21	$ 180	$ 453

The following are the undiscounted maturities of the long-term loans receivable and interest payments from Capital Power at December 31, 2011:

	2012	2013	2014	2015	2016	2017 and thereafter	Total
Long-term loans receivable from Capital Power (note 16)	$ 25	$ 14	$ 8	$ 9	$ 139	$ 184	$ 379
Interest payments on loans receivable from Capital Power	25	23	22	22	16	16	124
	$ 50	$ 37	$ 30	$ 31	$ 155	$ 200	$ 503

The payments from Capital Power fund a portion of the Company's contractual debt obligations. Should Capital Power be unable to make its scheduled payments to EPCOR or reduces its distributions, then the Company will rely more heavily on its credit facilities and its ability to issue medium-term notes or potentially sell a portion of its interest in Capital Power to fund its obligations.

34. 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 Company's growth strategy. 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 year.

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 and shareholder's equity. The following table represents the Company's total capital:

	2012	2011
Loans and borrowing (including current portion) (note 24)	$ 1,970	$ 1,699
Cash and cash equivalents	(232)	(316)
Net debt	1,738	1,383
Total equity	2,234	2,351
Total capital	$ 3,972	$ 3,734

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

- 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 if the Company's credit rating falls below investment grade; and
- Limitation on external debt issued by subsidiaries.

These capital restrictions are defined in accordance with the respective agreements. For the year ended December 31, 2012, the Company complied with all externally imposed capital restrictions.

35. Commitments and contingencies

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

(a) The Company has committed to various distribution and transmission projects through 2013, as directed by the AESO. The total estimated project costs are $13 million (2011 – $40 million). The Company has incurred costs of $2 million (2011 – $23 million).

(b) 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.

(c) Water Arizona maintains agreements with the Central Arizona Water Conservation District for the purchase and transportation of water. These agreements are for terms of 100 years expiring at the end of 2107. Under the terms of these agreements, certain minimum payments of approximately $0.5 million are due each year in order to maintain the agreements until they expire. Additional payment obligations related to orders placed in the fall of each year for water to be purchased and transported the following year, commit the Company only for the amount of the water ordered. The obligations are $8 million in total from 2013 through 2017 and $3 million in aggregate thereafter.

(d) The Company has entered into an agreement for billing and customer care services for Water Arizona and Water New Mexico. The contract term is ten years, expiring on August 31, 2021. The payments are estimated to be $21 million in total from 2013 through 2017 and $10 million in aggregate thereafter.

36. Guarantees

At December 31, 2012, the Company had letters of credit outstanding of $139 million (2011 – $272 million) to meet the credit requirements of electricity market participants and to meet conditions of certain service agreements.

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 statement of financial position.

The Company has no other material guarantee obligations outstanding in respect of third parties at December 31, 2012.

37. Segment disclosures

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 the treatment of wastewater within Edmonton and other communities throughout Western Canada and the Southwestern U.S. The separate Canadian and U.S. operating segment results are reviewed by the Company's Chief Executive Officer. However significant judgment is applied in determining the appropriate reportable segment. In particular, these two operating segments are aggregated as one reportable segment since both operating segments offer the same water and wastewater services, the processes to treat water and wastewater are similar in both operating segments, the customer bases for each operating segment are similar, both segments operate under similar rate regulations and the margins earned by both segments are similar.

Distribution and Transmission

Distribution and Transmission is involved in the transmission and distribution of electricity within Edmonton. This segment also provides complementary commercial services including the maintenance and repair of the City-owned street lighting and transportation support facilities.

Energy Services

Energy Services is primarily involved in the provision of regulated tariff electricity service and default supply electricity services to residential, small commercial and agricultural customers in Alberta.

Corporate

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

Business information

Year ended December 31, 2012	Water Services	Distribution & Transmission	Energy Services	Corporate	Intersegment Elimination	Consolidated
External revenues and other income	$ 465	$ 351	$ 1,114	$ 29	$ -	$ 1,959
Inter-segment revenue	-	164	11	-	(175)	-
Total revenue and other income	465	515	1,125	29	(175)	1,959
Electricity purchases and system access fees	-	134	1,024	-	(152)	1,006
Other raw materials and operating charges	108	45	1	1	(10)	145
Staff costs and employee benefits expenses	111	92	22	56	-	281
Depreciation and amortization	65	46	8	14	-	133
Franchise fees and property taxes	21	63	-	-	-	84
Other administrative expenses	20	12	26	12	(13)	57
Foreign exchange loss	-	-	-	2	-	2
Operating expenses	325	392	1,081	85	(175)	1,708
Operating income (loss) before corporate charges	140	123	44	(56)	-	251
Corporate charges (income)	33	39	15	(87)	-	-
Operating income	107	84	29	31	-	251
Finance expense	(71)	(31)	(9)	(5)	-	(116)
Equity share of income of Capital Power	-	-	-	41	-	41
Loss on sale of a portion of investment in Capital Power	-	-	-	(36)	-	(36)
Impairment of investment in Capital Power	-	-	-	(124)	-	(124)
Income tax (expense) recovery	(4)	-	(5)	11	-	2
Net income	$ 32	$ 53	$ 15	$ (82)	$ -	$ 18
Total assets	$ 2,556	$ 1,564	$ 235	$ 1,086	$ (17)	$ 5,424
Investment in Capital Power	-	-	-	621	-	621
Total liabilities	2,064	943	185	15	(17)	3,190
Capital additions	145	222	5	7	-	379

Year ended December 31, 2011	Water Services	Distribution & Transmission	Energy Services	Corporate	Intersegment Elimination	Consolidated
External revenues and other income	$ 312	$ 330	$ 1,152	$ 39	$ -	$ 1,833
Inter-segment revenue	-	152	11	-	(163)	-
Total revenue and other income	312	482	1,163	39	(163)	1,833
Electricity purchases and system access fees	-	143	1,077	-	(144)	1,076
Other raw materials and operating charges	82	40	1	-	(8)	115
Staff costs and employee benefits expenses	85	84	19	48	-	236
Depreciation and amortization	41	41	9	14	-	105
Franchise fees and property taxes	16	61	-	-	-	77
Other administrative expenses	11	12	26	7	(11)	45
Foreign exchange gain (loss)	1	-	-	(10)	-	(9)
Operating expenses	236	381	1,132	59	(163)	1,645
Operating income (loss) before corporate charges	76	101	31	(20)	-	188
Corporate charges (income)	24	32	15	(71)	-	-
Operating income	52	69	16	51	-	188
Finance expense	(48)	(31)	(8)	(21)	-	(108)
Equity share of income of Capital Power	-	-	-	90	-	90
Loss on sale of a portion of and net loss on dilutions of investment in Capital Power	-	-	-	(24)	-	(24)
Income tax (expense) recovery	-	-	(2)	-	-	(2)
Net income	$ 4	$ 38	$ 6	$ 96	$ -	$ 144
Total assets	$ 1,795	$ 1,174	$ 279	$ 1,801	$ (17)	$ 5,032
Investment in Capital Power	-	-	-	987	-	987
Total liabilities	1,441	807	244	206	(17)	2,681
Capital additions	108	188	1	41	-	338

Geographic information

	Year ended December 31, 2012				Year ended December 31, 2011			
	Canada	U.S.	Inter-segment eliminations	Total	Canada	U.S.	Inter-segment eliminations	Total
External revenues and other income	$ 1,833	$ 126	$ -	$ 1,959	$ 1,827	$ 6	$ -	$1,833
Inter-segment Revenues	175	-	(175)	-	163	-	(163)	-
Total revenues and other income	$ 2,008	$ 126	$ (175)	$ 1,959	$ 1,990	$ 6	$ (163)	$1,833

Non-current assets

	December 31, 2012	December 31, 2011
Canada	$ 4,109	$ 4,267
U.S.	711	54
	$ 4,820	$ 4,321