# EPCOR Utilities Inc.
# Interim Report
# March 31, 2007

## Management’s Discussion and Analysis

This management’s discussion and analysis (“MD&A”), dated May 3, 2007, should be read in conjunction with the unaudited interim consolidated financial statements of EPCOR Utilities Inc. (hereinafter the “Company”, “EPCOR”, “we”, “our” or “us”) for the three months ended March 31, 2007 and 2006 and in conjunction with the audited consolidated financial statements and MD&A for the year ended December 31, 2006. In accordance with its terms of reference, the Audit Committee of the Company’s Board of Directors reviews the contents of the MD&A and recommends its approval by the Board of Directors. The Board of Directors has approved this MD&A upon the recommendation of the Audit Committee.

### FORWARD-LOOKING STATEMENTS

Certain information in this MD&A is forward-looking and related to anticipated financial performance, events and strategies. When used in this context, words such as “will”, “anticipate”, “believe”, “plan”, “intend”, “target”, “expect” or similar words suggest future outcomes. By their nature, such statements are subject to significant risks and uncertainties, which could cause EPCOR’s actual results and experience to be materially different than the anticipated results. Such risks and uncertainties include, but are not limited to, operating performance, commodity prices and volumes, load settlement, regulatory and government decisions, weather and economic conditions, competitive pressures, construction risks, obtaining financing and the performance of partners, contractors and suppliers.

Readers are cautioned not to place undue reliance on forward-looking statements as actual results could differ materially from the plans, expectations, estimates or intentions expressed in the forward-looking statements. Except as required by law, EPCOR disclaims any intention and assumes no obligation to update any forward-looking statement even if new information becomes available, as a result of future events or for any other reason.

### SIGNIFICANT EVENTS

#### Sale of power purchase arrangement

On January 1, 2007, we sold a 10% interest in the Battle River Power Syndicate Agreement (“Battle River PSA”) for cash proceeds of $59 million resulting in a pre-tax gain of $34 million. The associated income taxes were $4 million of expense and $7 million of refundable taxes which were charged to retained earnings. This sale was pursuant to the purchase and sale agreement entered into in June 2006 whereby EPCOR will sell its Battle River Power Purchase Arrangement (“Battle River PPA”) and related interest in the Battle River PSA to ENMAX Corporation (“ENMAX”) over a four-year period ending in January 2010. An initial 55% interest was sold for cash proceeds of $343 million on June 5, 2006.

## Energy Services reorganization

On January 1, 2007, we reorganized our two subsidiaries within the Energy Services segment that operate our regulated retail business. As part of the transactions, one of the subsidiaries, which was previously exempt from income taxes became subject to income taxes under the Income Tax Act. Upon becoming taxable the subsidiary recognized future income tax assets of $11 million and a corresponding reduction in income tax expense.

## Keephills 3

On February 26, 2007, EPCOR and TransAlta Corporation (“TransAlta”) announced their decision to build Keephills 3, a 450 megawatts (“MW”) supercritical coal-fired generation plant at TransAlta’s Keephills site. Construction is expected to be completed by 2011. Our 50% committed share of the total capital cost is estimated to be $820 million. In addition, EPCOR and TransAlta have indemnified each other for up to $115 million during construction in the event that either party makes payments to the turbine supplier on behalf of the other party.

# CONSOLIDATED RESULTS OF OPERATIONS

## Net income

| (Unaudited, $ millions) | | |
|---|---|---|
| **Net income for the quarter ended March 31, 2006** | **$** | **186** |
| Gain on sale of 10% interest in Battle River PSA on January 1, 2007 | | 30 |
| Impact of recording a net future income tax asset associated with the Energy Services reorganization on January 1, 2007 | | 11 |
| Lower financing expenses and preferred share dividends, excluding Power LP financing | | 6 |
| Higher income from Power LP | | 6 |
| Lower administration expenses, excluding Power LP administration | | 3 |
| Lower PPA availability incentive income and capacity payments | | (5) |
| Unrealized fair value changes in financial and non-financial derivative instruments, excluding Power LP | | (25) |
| Impact of recording a net future income tax asset associated with the restructuring of EPCOR Generation Inc. on January 3, 2006 | | (117) |
| Other | | 3 |
| Decrease in net income | | (88) |
| **Net income for the quarter ended March 31, 2007** | **$** | **98** |

Net income was $98 million for the three months ended March 31, 2007 compared to $186 million for the same period in 2006.

- Financing expenses, excluding EPCOR Power LP (“Power LP”) financing, decreased primarily due to interest earned on higher cash balances, repayment in the third quarter of 2006 of a $98 million loan issued under the three-year credit facility and scheduled repayments of obligations to the City of Edmonton. Preferred share dividends decreased due to the redemption of $150 million of subsidiary preferred shares on June 30, 2006.

- Net income from Power LP increased primarily due the fair value changes in the natural gas supply contracts for its Ontario generation plants for the three months ended March 31, 2007. These adjustments were due to the implementation of the new accounting standard for financial instruments that was implemented, as required, on January 1, 2007. The contracts did not qualify for the designation as contracts used for the purpose of receipt of natural gas in accordance with our expected purchase or usage requirements under the accounting standard and therefore had to be measured at fair value. There was no comparable adjustment in 2006 as the new accounting standard is effective January 1, 2007. The opening fair value adjustment at January 1, 2007 was recorded in retained earnings. See “New Accounting Standards in 2007”.

- Administration expenses, excluding Power LP’s administration expenses, were lower primarily due to a valuation adjustment to the Company’s liability for its Long-Term Incentive Plan (“LTIP”) which is a notional stock option plan for senior executives and managers. The adjustment reflected a reduction in the estimated LTIP liability as a result of the formula-based valuation of the plan at the end of the current quarter.

- Availability incentive income on the generation units operating under a Power Purchase Arrangement (“PPA”) was lower in the first quarter of 2007 compared to the same period in 2006 because the incentive income recognized in the first quarter of 2006 was based on higher anticipated annual generation as no outages were planned for the year at that time. Capacity payments earned under the PPA were also lower due to a lower tax recovery component of the payments resulting from lower income tax rates compared to the same period in the prior year.

- The unrealized fair value changes in derivative financial and non-financial instruments include unfavourable changes on Alberta merchant and wholesale positions, forward foreign currency contracts, and the Joffre contract-for-differences (“CfD”). The unfavourable change in the Alberta merchant and wholesale position was due to an increase in financial sales contracts which were not designated as hedges for accounting purposes combined with higher Alberta forward electricity prices than in the prior year. The increase in the volume of financial sales contracts not qualifying for hedge accounting was due to decreased generation as a result of our reduced interest in the Battle River PSA. The decrease in the forward foreign currency contracts was due to the prior year’s unrealized gains on contracts no longer held in 2007. The decrease in the Joffre CfD was due to higher forward natural gas prices compared to the forward prices in the first quarter of 2006.

- The January 3, 2006 reorganization of the Generation subsidiaries resulted in recognition of a future income tax asset associated with additional deductions available for income tax purposes, partly offset by the write-off of future income tax balances associated with the Alberta government’s Payment in Lieu of Tax Regulation, thereby increasing income in 2006 by $117 million. There was no corresponding tax adjustment in the Generation segment in 2007.

## Revenues

| (Unaudited, $ millions) | | |
|---|---|---|
| **Revenues for the quarter ended March 31, 2006** | **$** | **812** |
| Higher energy sales | | 105 |
| Higher Power LP revenues | | 51 |
| Unrealized fair value changes in derivative financial and non-financial instruments | | (69) |
| Increase in revenues | | 87 |
| **Revenues for the quarter ended March 31, 2007** | **$** | **899** |

Consolidated revenues for the first quarter of 2007 were $87 million higher than for the same period of the prior year due to the following:

- Energy sales increased due to higher gas trading activities, partly offset by a decrease in generation relating to our reduced interest in the Battle River PSA, and decreased generation availability incentive income and capacity payments.

- Revenues from Power LP were $143 million in the first quarter of 2007 compared to $92 million for the same period in 2006. Revenues increased primarily due to the acquisition of Primary Energy Ventures LLC ("PEV") on November 1, 2006 and Frederickson Power LP ("Frederickson") on August 1, 2006.

- Unrealized fair value changes on derivative financial instruments decreased energy revenues by $69 million in the first quarter of 2007 compared to 2006 due to increasing Ontario forward electricity prices on financial sales contracts in the Ontario market, and a combination of increasing Alberta forward electricity prices and higher volumes of financial sales contracts in the Alberta market.

## Capital spending and investment

| (Unaudited, $ millions)<br>Three months ended March 31 | | 2007 | | 2006 |
|---|---|---|---|---|
| Generation | $ | 42 | $ | 13 |
| Distribution and Transmission | | 12 | | 11 |
| Energy Services | | 3 | | 1 |
| Water Services | | 14 | | 11 |
| Corporate – other | | 3 | | 2 |
| | $ | 74 | $ | 38 |

Capital expenditures for property plant and equipment were higher in the first quarter of 2007 compared to the same period in 2006 primarily due to the Keephills 3 and Clover Bar generation projects which commenced in the first quarter of 2007. In December 2006, the Alberta Energy and Utilities Board ("EUB") approved our proposal to construct three natural gas-fired peaking power generation units for an aggregate gross generating capacity of 240 MW at our Clover Bar site in northeast Edmonton.

In the first quarter of 2007, Distribution and Transmission commenced construction of the new high voltage transmission line and substation project, which will supply electricity to downtown Edmonton. Water Services' construction on the EL Smith water treatment plant expansion continued in the quarter. Both projects are scheduled for completion in 2008.

## SEGMENT RESULTS

### Generation

| Three months ended March 31 | 2007 | 2006 |
|---|---|---|
| **Generation results** (including intersegment transactions) | | |
| (Unaudited, $ millions) | | |
| Revenues | $ 244 | $ 202 |
| Expenses | 117 | 98 |
| **Operating income** | **$ 127** | **$ 104** |

| (Unaudited, $ millions) | |
|---|---|
| **Operating income for the quarter ended March 31, 2006** | **$ 104** |
| Higher operating income from Power LP | 39 |
| Unrealized fair value changes in derivative instruments | (3) |
| Lower PPA availability incentive income and capacity payments | (8) |
| Other | (5) |
| Increase in operating income | 23 |
| **Operating income for the quarter ended March 31, 2007** | **$ 127** |

Generation's operating income for the quarter increased by $23 million over the same quarter in 2006 due to the following:

- Power LP contributed $81 million of operating income in the first quarter of 2007 compared to $42 million for the first quarter of 2006. Power LP's revenues and expenses were higher for the three months ended March 31, 2007 compared to the prior year period primarily due to the acquisition of PEV on November 1, 2006 and Frederickson on August 1, 2006.

  As well, implementation of the new accounting standards for financial instruments, effective January 1, 2007, resulted in a reduction in expenses arising from positive unrealized fair value changes in the natural gas supply contracts for Power LP's Ontario generation plants for the three months ended March 31, 2007. Fair value changes for accounting purposes in the natural gas supply contracts are not necessarily representative of changes in the economic value of these contracts when considered in conjunction with the economically hedged item, such as future natural gas requirements and future power sales.

- The generation from the Joffre plant is subject to a CfD which is a financial agreement whereby the difference between the Alberta Electric System Operator ("AESO") pool price and the AECO-C price (Alberta gas trading price), and the contracted price, is remitted by one counterparty to the other. Revenues and expenses related to the unrealized fair value changes on the CfD increased $2 million and $5 million respectively, over the corresponding period in 2006. The net decrease in the unrealized fair value changes recognized in the first quarter of 2007 on this financial contract was due to higher forward natural gas prices compared to the forward prices in the first quarter of 2006.

## Distribution and Transmission

| Three months ended March 31 | | 2007 | | 2006 |
|---|---|---|---|---|
| **Distribution and Transmission results** (including intersegment transactions) | | | | |
| (Unaudited, $ millions) | | | | |
| Revenues | $ | 59 | $ | 61 |
| Expenses | | 48 | | 52 |
| **Operating income** | **$** | **11** | **$** | **9** |

There were no material changes in revenues, expenses and operating income, for the current quarter compared to the same period in the prior year.

## Energy Services

| Three months ended March 31 | | 2007 | | 2006 |
|---|---|---|---|---|
| **Energy Services results** (including intersegment transactions) | | | | |
| (Unaudited, $ millions) | | | | |
| Revenues | $ | 616 | $ | 572 |
| Expenses | | 607 | | 536 |
| **Operating income** | **$** | **9** | **$** | **36** |

| (Unaudited, $ millions) | | |
|---|---|---|
| **Operating income for the quarter ended March 31, 2006** | **$** | **36** |
| Higher Alberta natural gas margin | | 3 |
| Lower Alberta electricity margins | | (6) |
| Unrealized fair value changes in derivative instruments | | (28) |
| Other | | 4 |
| Decrease in operating income | | (27) |
| **Operating income for the quarter ended March 31, 2007** | **$** | **9** |

Energy Services' operating income for the three-month period ended March 31, 2007 was $27 million lower than it was for the same period in 2006 due to the net impact of the following:

- Alberta natural gas margins were higher due to higher priced contracted gas sales.
- Alberta electricity margins for the Regulated Rate Tariff ("RRT") customers were lower due to changes in the Energy Price Setting Plan ("EPSP") effective July 1, 2006. The EUB-approved EPSP sets out the price setting mechanism for determining the regulated rates to be charged to these customers for electricity, distribution and transmission services. The Alberta electricity margins were also impacted by unfavourable energy settlements compared to customer billings. Due to the imprecision in customer consumption data received from load settlement agents and the time lags inherent in the resettlement process, we use estimates for determining the amount of energy consumed but not yet billed. The first quarter variance is within an acceptable range for this estimate and could reverse with the receipt of future resettlement information.
- Energy Services' energy revenues and expenses, excluding unrealized fair value changes, increased by $115 million and $116 million, respectively, due to higher gas trading activities, partly offset by lower Alberta electricity revenues and expenses due to our reduced interest in the Battle River PSA.
- The unrealized fair value changes in our financial electricity contracts were unfavourable

compared to the prior year due to a combination of more financial sales contracts not designated as hedges for accounting purposes and higher Alberta forward electricity prices. These financial sales contracts hedge anticipated energy revenues on an economic basis. The volume of these instruments that were fair valued was higher in 2007 due to decreased generation as a result of our reduced interest in the Battle River PSA.

Unrealized fair value losses on derivative instruments decreased energy revenues by $71 million for the first quarter of 2007 compared to 2006 due to increasing Ontario forward electricity prices on financial sales contracts, and a combination of increasing Alberta forward electricity prices on financial sales contracts and higher volumes. Unrealized fair value changes on financial purchase contracts decreased energy purchases $43 million in 2007 compared to 2006 due to increasing Ontario forward electricity prices. Unrealized fair value changes in derivative instruments recorded for accounting purposes are not necessarily representative of the changes in economic value when considering them in conjunction with the economically hedged item such as future power supply.

## Water Services

| Three months ended March 31 | 2007 | 2006 |
|---|---|---|
| **Water Services results** (including intersegment transactions) | | |
| (Unaudited, $ millions) | | |
| Revenues | $ 43 | $ 43 |
| Expenses | 35 | 34 |
| **Operating income** | **$ 8** | **$ 9** |

There were no material changes in revenues, expenses and operating income for the current quarter compared to the same period in the prior year.

## CONSOLIDATED BALANCE SHEETS

Significant changes in consolidated assets are outlined below:

| | March 31, 2007 | December 31, 2006 | Increase (decrease) $ millions | Explanation |
|---|---|---|---|---|
| Cash and cash equivalents | $ 289 | $ 260 | $ 29 | Refer to cash flows summary below. |
| Accounts receivable (including income taxes recoverable) | 441 | 644 | (203) | Reflects two months of Alberta wholesale electricity settlements and Genesee generation revenues in the December 31, 2006 balance compared to one month at March 31, 2007. Sales were lower due to lower wholesale electricity prices in the first quarter of 2007 compared with the last quarter of 2006. |
| Derivative instruments asset (current) | 128 | 26 | 102 | Reflects implementation of new financial instruments accounting standards for physical power and natural gas purchase and sales contracts and derivatives used in cash flow hedges of electricity. |
| Other current assets | 69 | 73 | (4) | |
| Property, plant and equipment | 3,936 | 3,906 | 30 | Reflects first quarter capital expenditures partly offset by depreciation and amortization expense. |
| Power purchase arrangements (“PPA”s) | 722 | 757 | (35) | Reflects sale of 10% interest in Battle River PSA and amortization of PPAs. |
| Contract and customer rights and other intangible assets | 202 | 207 | (5) | |
| Derivative instruments asset (non- current) | 164 | 20 | 144 | Reflects implementation of new financial instruments accounting standards for physical power and natural gas purchase and sale contracts and derivatives used in cash flow hedges of electricity. |
| Future income tax asset (non-current) | 163 | 127 | 36 | Reflects increase in deductions available for tax purposes resulting from implementation of new financial instruments accounting standards and the Energy Services reorganization of January 1, 2007. |
| Goodwill | 184 | 183 | 1 | |
| Other assets | 169 | 180 | (11) | Reflects reclassification of deferred financing costs to long-term debt in accordance with the new financial instruments accounting standard. |

Significant changes in consolidated liabilities and shareholder's equity are outlined below:

| | **March 31, 2007** | **December 31, 2006** | **Increase (decrease) $ millions** | **Explanation** |
|---|---|---|---|---|
| Short-term debt | $ 214 | $ 216 | $ (2) | |
| Derivative instruments liability (current) | 132 | 24 | 108 | Reflects implementation of new financial instruments accounting standards for derivatives used in cash flow hedges of electricity and for physical power and natural gas purchase and sales contracts. |
| Accounts payable and accrued liabilities | 405 | 603 | (198) | Reflects two months of Alberta wholesale electricity settlements in the December 31, 2006 balance compared to one month at March 31, 2007. In addition, energy purchases were lower due to lower wholesale electricity prices in the first quarter of 2007 compared with the last quarter of 2006. |
| Other current liabilities | 133 | 129 | 4 | |
| Long-term debt (including current portion) | 2,118 | 2,179 | (61) | Reflects ongoing scheduled debt repayments and reclassification of deferred financing costs from other assets in accordance with new financial instruments accounting standard. |
| Derivative instruments liability (non-current) | 148 | 27 | 121 | Reflects implementation of new financial instruments accounting standards for derivatives used in cash flow hedges of electricity and for physical power and natural gas purchase and sales contracts. |
| Future income tax liability (non-current) | 93 | 80 | 13 | |
| Other non-current liabilities | 126 | 131 | (5) | |
| Non-controlling interests | 848 | 751 | 97 | Reflects opening adjustment upon implementation of financial instruments accounting standards attributable to non-controlling interests, and non-controlling interests' share of Power LP income less distributions. |
| Shareholder's equity | 2,250 | 2,243 | 7 | Reflects net income and adjustments to retained earnings upon implementation of financial instruments accounting standards, offset by common share dividends and refundable income taxes. Also reflects adjustment to accumulated other comprehensive income upon implementation of financial instruments accounting standards and other comprehensive income for the quarter. |

## LIQUIDITY AND CAPITAL RESOURCES

Cash inflows (outflows) are summarized below:

| | Three months ended March 31, 2007 | Three months ended March 31, 2006 | Increase (decrease) $ millions | Explanation |
|---|---|---|---|---|
| Operating | $ 150 | $ 171 | $ (21) | Reflects change in non-current items, primarily increased long-term receivables. |
| Investing | (25) | (46) | 21 | Reflects sale of interest in Battle River PSA, partly offset by higher capital expenditures, primarily Keephills 3 and Clover Bar generation projects. |
| Financing | (96) | (88) | (8) | Net financing outlays were higher in 2007 due to distributions to non-controlling interests partly offset by lower scheduled debt repayments as period opening debt balances were lower in 2007. |

## NEW ACCOUNTING STANDARDS IN 2007

As we described in EPCOR's most recent annual MD&A, the Company has adopted accounting policies in accordance with the following new accounting standards.

### Financial instruments, hedges and comprehensive income

On January 1, 2007, we adopted the Canadian Institute of Chartered Accountants' new accounting standards "Financial Instruments - Recognition and Measurement", "Financial Instruments – Disclosure and Presentation, "Hedges", and "Comprehensive Income".

As required by the new accounting standards, our comparative interim financial statements have not been restated, except to reclassify the foreign currency translation gains and losses on net investments in self-sustaining foreign operations from the cumulative translation adjustment account to accumulated other comprehensive income.

A statement called Consolidated Statement of Comprehensive Income has been added to our consolidated financial statements. This statement includes net income and the components of other comprehensive income such as unrealized foreign exchange gains and losses arising from the translation of self-sustaining foreign operations and the effective portion of the changes in the fair value of derivative instruments used in cash flow hedges of electricity sales and purchases and of anticipated foreign currency cash flows. As the foreign exchange gains and losses are realized or the hedged item of the cash flow hedge affects income, these items of other comprehensive income are reclassified to the income statement. Other comprehensive income is intended to capture the changes in the fair value of the financial instruments, derivatives or translated balances, which would not otherwise be recorded in the financial statements.

Each component of this new statement is recorded net of income taxes. Accumulated other comprehensive income is a new component of shareholder's equity.

### Financial instruments

All financial and non-financial derivative instruments are recorded at fair value in the Consolidated Balance Sheets, including derivatives that are used to manage our risks, and are specifically designated and qualify for hedge accounting. At March 31, 2007 the fair value of these instruments was $94 million and is included in derivative instruments asset and derivative instruments liability in the Consolidated Balance Sheets. Prior to January 1, 2007, the fair value of financial derivative instruments that qualified for hedge accounting was not recorded in the balance sheet and was disclosed as an off-balance sheet item. However, non-financial derivative instruments designated as contracts used for the purpose of receipt or delivery of a non-financial item in accordance with our expected purchase, sale or usage requirements continue to be recorded in income on their settlement date.

In addition, certain physical power and natural gas purchase and sales contracts are not designated as contracts used in accordance with our expected purchase requirements, as defined in the accounting standard, and therefore are recorded at fair value in the balance sheet. The fair valuation of fuel supply contracts in Power LP resulted in an increase in derivative assets of $140 million, a reduction in fuel costs of $44 million and an increase in non-controlling interests of $97 million. The unrealized fair value adjustment for these contracts as at January 1, 2007 of $20 million net of income taxes and non-controlling interests was recorded in opening retained earnings for the period. The fair valuation of other physical power and natural gas purchase and sales contracts resulted in an increase in derivative assets of $36 million and derivative liabilities of $35 million at March 31, 2007, and an increase in revenues of $1 million for the quarter.

In accordance with the new accounting standard we have reclassified $15 million of debt issue costs from other assets to long-term debt effective January 1, 2007 and amortized them using the effective interest rate method. Previously debt issue costs were amortized on a straight-line basis over the life of the associated debt. Also in accordance with the new accounting standard, the Company expenses any transaction costs on financial instruments classified as “held for trading”.

All financial assets, except for those classified as held-to-maturity, loans and receivables are measured at their fair values. All financial liabilities are held at amortized cost. All derivative instruments, except for those designated as contracts used in accordance with our expected purchase and sale requirements, are classified as held for trading and measured at fair value.

### Hedges

As of January 1, 2007 the changes in the fair value of the effective portion of the financial derivative contracts used to manage our energy portfolio and designated as accounting hedges, are recorded in other comprehensive income. The ineffective portion of the contracts is recorded in net income. Historically, such financial contracts were recorded in the income statement as they settled.

Opening 2007 retained earnings decreased $8 million net of income taxes to recognize the fair value of the ineffective portion of hedging financial instruments at December 31, 2006. The transition adjustment to opening accumulated other comprehensive income included unrealized losses net of income taxes of $42 million related to cash-flow hedging relationships and $1 million of unrealized gains net of non-controlling interests and income taxes related to previously discontinued cash flow hedges no longer deferred in derivative instruments asset and liability in the Consolidated Balance Sheet.

## CRITICAL ACCOUNTING ESTIMATES

Implementation of the new accounting standard on financial instruments has required us to record more of our derivative instruments at fair value than in the past, which involves a greater use of estimates. The most significant item requiring fair valuation for the first time was Power LP's natural gas supply contracts for its Ontario plants. This valuation reflects management's best estimates considering various factors including closing exchange or over-the-counter quotations, estimates of futures prices and foreign exchange rates, time value and volatility. In illiquid or inactive markets, we use appropriate price modeling to estimate fair value. It is possible that the assumptions used in establishing fair value amounts will differ from actual prices and the impact of such variations could be material.

## RISK MANAGEMENT

This section should be read in conjunction with the Risk Management section of the most recent annual MD&A. EPCOR faces a number of risks including electricity price and volume risk, natural gas price and volume risk, operational risk, government and regulatory risk, supply risk of acquired PPAs, credit risk, environmental risk, project risk, availability of people risk, weather risk, foreign exchange risk, conflicts of interest risk, and general economic conditions and business environment risks. The Company employs active programs to manage these risks.

On April 25, 2007, the Canadian Environment Minister announced a new regulatory framework to reduce greenhouse gas emissions and air pollution in Canada. The Canadian government has set targets of a 20% reduction in greenhouse gases by 2020 and a 50% reduction in air pollution by 2015. The Company is an emitter of carbon dioxide (a greenhouse gas), nitrogen oxide and sulphur dioxide which are all targeted for reduction under the proposed new legislation. The Company complies, in all material respects, with current federal, provincial, state and local environmental legislation and guidelines. The operational and financial impact to the Company of the new regulatory framework cannot be determined until further details are announced.

As part of its ongoing risk management practices, the Company reviews current and proposed transactions to consider their impact on the risk profile of the Company. There have been no other material changes to the risk profile or risk management strategies of EPCOR as described in the annual MD&A for 2006.

## INTERNAL CONTROLS OVER FINANCIAL REPORTING

The Company continues to document and review the design of internal controls over financial reporting of the Primary Energy Ventures business that was acquired by Power LP in the fourth quarter of 2006. We expect to complete the documentation and review of such design by the end of the second quarter of 2007.

There were no changes in the Company's internal controls over financial reporting that have occurred since December 31, 2006 that have materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting.

## OUTLOOK

Excluding the gain on sale of the interest in the Battle River PSA and the impact of fair value changes, earnings are expected to be slightly lower for the next three quarters, in part due to normal seasonal variances. The implementation of the new accounting standard on financial instruments is expected to increase the volatility of our earnings, which may not be representative of the performance of the underlying business and has no impact on our cash flows.

## QUARTERLY RESULTS

| Quarter ended | Revenues | Net income from continuing operations | Net income (loss) from discontinued operations | Net income |
|---|---|---|---|---|
| | | (Unaudited, $ millions) | | |
| March 31, 2007 | $ 899 | $ 98 | $ - | $ 98 |
| December 31, 2006 | 728 | 16 | 1 | 17 |
| September 30, 2006 | 702 | 47 | 9 | 56 |
| June 30, 2006 | 689 | 383 | - | 383 |
| March 31, 2006 | 812 | 186 | - | 186 |
| December 31, 2005 | 866 | 46 | (9) | 37 |
| September 30, 2005 | 582 | 63 | 22 | 85 |
| June 30, 2005 | 576 | 46 | 10 | 56 |

Events for 2007, 2006 and 2005 quarters that have significantly impacted net income from continuing operations and net income and the comparability between quarters are:

- December 31, 2006 fourth quarter results include unrealized fair value decreases in derivative financial instruments which were not designated as hedges for accounting purposes, resulting from higher forward market prices. In addition, income from Power LP included unrealized foreign exchange losses on the translation of US dollar debt. These events were partly offset by increased generation from a short-term tolling arrangement with Calpine Power Income Fund, higher generation incentive income and realized gains on foreign exchange forward contracts.
- September 30, 2006 third quarter results include a net income increase from discontinued operations of $10 million for the reduction of the Clover Bar asset retirement obligation offset by reduced Alberta electricity margins from the Battle River and Sundance PPAs resulting from the sale of partial interests in these agreements in the second quarter of 2006.
- June 30, 2006 second quarter results include the sale of a 55% interest in the Battle River PSA and related transactions which contributed $327 million to net income. The regulatory decisions for the 2005/2006 distribution and transmission tariffs and the RRT non-energy charge were received in the second quarter of 2006 resulting in a $10 million increase in net income. Future income tax assets and liabilities were adjusted to reflect the corporate income tax rate reductions that were enacted by the governments of Alberta

and Canada in the quarter. These tax adjustments reduced net income by $16 million.

- March 31, 2006 first quarter results include the tax impact of the Generation reorganization whereby a Generation subsidiary became subject to federal and provincial income taxes rather than the PILOT Regulation. As a result, additional deductions are available for income tax purposes and the net tax effect was recognized as non-current future income tax assets in the balance sheet with a corresponding increase in net income of $117 million. In addition, unrealized fair value changes in derivative financial instruments increased net income by $14 million.

- December 31, 2005 fourth quarter results include the impact of reduced Alberta electricity margins as margins on new and renewed electricity contracts decreased.

- September 30, 2005 third quarter results include a net income increase of approximately $17 million for the Clover Bar PPA termination payment partly offset by the write-down of the Clover Bar assets. The third quarter results also include gains of $13 million after income taxes on the sale of Alberta mid-market electricity contracts and settlement of litigation.

- June 30, 2005 second quarter results include the unrealized gains for fair value changes on energy supply contracts associated with Ontario electricity sales contracts that were sold during the quarter. These gains had previously been deferred in accordance with hedge accounting and were approximately $8 million after income taxes. June 30, 2005 second quarter results also include a full quarter's results of operations for the Genesee Phase 3 generation unit from its start-up date of March 1, 2005 of approximately $7 million after financing expenses and income taxes. As well, this quarter's results include decreased Alberta electricity margins of approximately $8 million after income taxes.

## Additional information

Additional information relating to EPCOR is available on SEDAR at www.sedar.com.

**EPCOR UTILITIES INC.**
**Consolidated Statements of Income**
**(Unaudited, in millions of dollars)**

| | Three months ended March 31 2007 | Three months ended March 31 2006 |
|---|---|---|
| **Revenues** | $ 899 | $ 812 |
| **Operating expenses (income):** | | |
| Energy purchases | 539 | 461 |
| Fuel | 26 | 29 |
| Operations, maintenance and administration | 102 | 93 |
| Franchise fee, property taxes and other taxes | 16 | 16 |
| Depreciation, amortization and asset retirement accretion | 63 | 58 |
| Foreign exchange gain | (3) | (3) |
| | 743 | 654 |
| | 156 | 158 |
| Gain on sale of power syndicate agreement (note 6) | 34 | - |
| **Income before financing expenses** | 190 | 158 |
| Financing expenses | 41 | 38 |
| **Income before income taxes and amounts in lieu of income taxes and non-controlling interests** | 149 | 120 |
| Income taxes and amounts in lieu of income taxes (reductions) (note 7) | (1) | (95) |
| **Income before non-controlling interests** | 150 | 215 |
| Non-controlling interests (note 8) | 52 | 29 |
| **Net income** | $ 98 | $ 186 |

See accompanying notes to consolidated financial statements.

**EPCOR UTILITIES INC.**
**Consolidated Balance Sheets**
**(In millions of dollars)**

| | March 31, 2007 (Unaudited) | December 31, 2006 (Audited) |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 289 | $ 260 |
| Accounts receivable | 431 | 643 |
| Income taxes recoverable | 10 | 1 |
| Inventories | 59 | 57 |
| Prepaid expenses | 8 | 12 |
| Derivative instruments asset | 128 | 26 |
| Future income tax asset | 2 | 1 |
| Current assets of discontinued operations | - | 3 |
| | 927 | 1,003 |
| Property, plant and equipment | 3,936 | 3,906 |
| Power purchase arrangements | 722 | 757 |
| Contract and customer rights and other intangible assets | 202 | 207 |
| Derivative instruments asset | 164 | 20 |
| Future income tax asset | 163 | 127 |
| Goodwill | 184 | 183 |
| Other assets | 167 | 178 |
| Non-current assets of discontinued operations | 2 | 2 |
| | $ 6,467 | $ 6,383 |
| **Liabilities and Shareholder's Equity** | | |
| Current liabilities: | | |
| Short-term debt | $ 214 | $ 216 |
| Accounts payable and accrued liabilities | 405 | 603 |
| Income taxes payable | 70 | 19 |
| Derivative instruments liability | 132 | 24 |
| Other current liabilities | 16 | 13 |
| Future income tax liability | 43 | 92 |
| Current portion of long-term debt | 49 | 63 |
| Current liabilities of discontinued operations | 4 | 5 |
| | 933 | 1,035 |
| Long-term debt | 2,069 | 2,116 |
| Derivative instruments liability | 148 | 27 |
| Other non-current liabilities | 126 | 127 |
| Future income tax liability | 93 | 80 |
| Non-current liabilities of discontinued operations | - | 4 |
| | 3,369 | 3,389 |
| Non-controlling interests (note 8) | 848 | 751 |
| Shareholder's equity | 2,250 | 2,243 |
| | $ 6,467 | $ 6,383 |

See accompanying notes to consolidated financial statements.

# EPCOR UTILITIES INC.
## Consolidated Statements of Changes in Shareholder's Equity
**(Unaudited, in millions of dollars)**

| | Three months ended March 31 2007 | Three months ended March 31 2006 |
|---|---|---|
| **Retained earnings** | | |
| Balance at beginning of period | $ 2,245 | $ 1,765 |
| Adjustment for changes in accounting policies (note 4) | 12 | - |
| Net income | 98 | 186 |
| Common share dividends paid | (32) | (31) |
| Refundable taxes | (7) | - |
| Balance at end of period | 2,316 | 1,920 |
| **Accumulated other comprehensive loss** | | |
| Balance at beginning of period | (2) | (8) |
| Adjustment for changes in accounting policies (note 4) | (41) | - |
| Other comprehensive loss | (23) | - |
| Balance at end of period | (66) | (8) |
| **Total shareholder's equity at end of period** | $ 2,250 | $ 1,912 |

See accompanying notes to consolidated financial statements.

## EPCOR UTILITIES INC.
## Consolidated Statements of Comprehensive Income
**(Unaudited, in millions of dollars)**

| | Three months ended March 31 2007 | Three months ended March 31 2006 |
|---|---|---|
| **Net income** | $ 98 | $ 186 |
| **Other comprehensive loss:** | | |
| Unrealized losses on derivative instruments designated as cash flow hedges (net of income taxes of $15 million) | (33) | - |
| Reclassification of losses on derivative instruments designated as cash flow hedges to net income (net of income taxes of $4 million) | 10 | - |
| | (23) | - |
| **Comprehensive income** | $ 75 | $ 186 |

See accompanying notes to consolidated financial statements.

**EPCOR UTILITIES INC.**
**Consolidated Statements of Cash Flows**
**(Unaudited, in millions of dollars)**

| | Three months ended March 31 | |
|---|---|---|
| | 2007 | 2006 |
| **Operating activities:** | | |
| Net income | $ 98 | $ 186 |
| Items not affecting cash: | | |
| Depreciation, amortization, and asset retirement accretion | 63 | 58 |
| Gain on sale of power syndicate agreement (note 6) | (34) | - |
| Non-controlling interests in EPCOR Power L.P. (note 8) | 49 | 24 |
| Fair value changes on derivative instruments | (20) | - |
| Other non-cash items | (4) | (20) |
| Future income taxes and amounts in lieu of income taxes | (9) | (101) |
| | 143 | 147 |
| Change in other non-current items | (13) | 4 |
| Net change in non-cash operating working capital | 20 | 20 |
| | 150 | 171 |
| **Investing activities:** | | |
| Property, plant, equipment and other assets | (74) | (38) |
| Net change in non-cash working capital | (10) | (8) |
| Proceeds on sale of power syndicate agreement (note 6) | 59 | - |
| | (25) | (46) |
| **Financing activities:** | | |
| Decrease in short-term debt | - | (28) |
| Principal payments on long-term debt | (42) | (29) |
| Distributions to non-controlling interests (note 8) | (22) | - |
| Common share dividends paid | (32) | (31) |
| | (96) | (88) |
| **Increase in cash and cash equivalents** | 29 | 37 |
| Cash and cash equivalents, beginning of period | 260 | 90 |
| **Cash and cash equivalents, end of period** | $ 289 | $ 127 |
| **Supplemental cash flow information:** | | |
| Interest paid | $ 38 | $ 36 |
| Income taxes paid net of income taxes recovered | 17 | 6 |

See accompanying notes to consolidated financial statements.

**EPCOR UTILITIES INC.**
**Notes to the Interim Consolidated Financial Statements**
**March 31, 2007**
**(Unaudited, in millions of dollars)**

## 1. Basis of presentation:

These unaudited interim consolidated financial statements of EPCOR Utilities Inc. (the Company or EPCOR) have been prepared in accordance with Canadian generally accepted accounting principles for interim financial statements and do not include all of the disclosures normally found in the Company's annual consolidated financial statements. These interim consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements for the year ended December 31, 2006.

These financial statements have been prepared following the same accounting policies and methods as those used in preparing the most recent annual financial statements except for the changes in accounting policies as described in note 4.

## 2. Nature of operations:

Interim results will fluctuate due to plant maintenance schedules, the seasonal demands for electricity and water, changes in energy prices and the timing and recognition of regulatory decisions. Consequently, interim results are not necessarily indicative of annual results.

## 3. Measurement uncertainty:

In accordance with Canadian generally accepted accounting principles, the Company uses estimates in preparing its consolidated financial statements. Interim consolidated financial statements necessarily employ a greater use of estimates than the annual consolidated financial statements.

## 4. Changes in accounting policies:

Commencing January 1, 2007, the Company adopted new accounting standards as issued by the Canadian Institute of Chartered Accountants (CICA) for Comprehensive Income, Equity, Financial Instruments and Hedges. In accordance with the new standards, the comparative interim financial statements have not been restated as a result of implementing the new accounting standards except to reclassify unrealized foreign currency translation gains and losses on net investments in self-sustaining foreign operations. They have been reclassified from the cumulative translation adjustment account to accumulated other comprehensive income, both within shareholder's equity.

## 4. Changes in accounting policies, (continued):

### Comprehensive income and equity

These new standards establish requirements for the reporting and presentation of comprehensive income which is composed of net income and other comprehensive income and for the presentation of equity and changes in equity due to the comprehensive income requirements. Other comprehensive income includes unrealized gains or losses arising from the translation of net investments in self-sustaining foreign operations and the changes in the fair value of the effective portion of derivative instruments used in cash flow hedges. Each component of the statement of comprehensive income is recorded net of income taxes. Accumulated other comprehensive income is a new component of shareholder’s equity.

### Financial instruments

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

Financial assets and financial liabilities held for trading are measured at fair value with the changes in fair value reported in earnings. Financial assets held to maturity, loans and receivables and financial liabilities other than those held for trading are measured at amortized cost. Available-for-sale financial assets are measured at fair value with changes in fair value reported in other comprehensive income until the financial asset is disposed of, or becomes impaired.

Transaction costs related to long-term debt are capitalized and amortized over the expected life of the instrument utilizing the effective interest method. Previously, these costs were deferred and amortized on a straight-line basis over the term of the debt. The effective interest method calculates the amortized cost of this financial liability and allocates the interest expense over the term of the debt using an effective interest rate.

All derivative instruments, including embedded derivatives, are recorded at fair value on the balance sheet as derivative instruments asset and derivative instruments liability unless exempted from derivative treatment as an expected purchase, sale or usage. All changes in their fair value are recorded in net income unless cash flow hedge accounting is used, in which case changes in fair value are recorded in other comprehensive income. The Company chose a transition date of January 1, 2003 for embedded derivatives and therefore will only be required to account separately for those embedded derivatives in any hybrid instruments issued, acquired or substantively modified after that date.

## 4. Changes in accounting policies (continued):

### Hedges

The hedging standards specify the criteria that must be met in order for hedge accounting to be applied. Hedge accounting enables the recording of gains, losses, revenues and expenses from derivative instruments in the same period as for those related to the hedged item. Hedge accounting may be applied for fair value hedges, cash flow hedges and hedges of foreign currency exposures of net investments in self-sustaining foreign operations if the criteria are met. These standards also specify that hedge accounting is discontinued when the hedge is no longer determined to be effective, the hedging item is sold or terminated, or upon the sale or early termination of the hedged item.

### Financial statement impact

Certain physical fuel purchase contracts are not designated as contracts used in accordance with our expected purchase requirements and, therefore, are measured at fair value. An opening adjustment to retained earnings to reflect the fair value of these contracts at January 1, 2007 has been recorded. Subsequent changes in the fair value of these contracts are reported in net income.

Qualifying cash flow hedges of electricity and natural gas sales and purchases have been established and the changes in the fair value of the effective portion of the associated derivative instruments have been reflected as an opening adjustment to accumulated other comprehensive income with subsequent changes to the effective portion included in other comprehensive income. The changes in the fair value of the ineffective portion of these derivatives are included in net income.

Prior to the adoption of these new standards, the unrealized losses on certain financial instruments which did not satisfy all the required conditions for hedge accounting were recorded as a derivative instruments asset in the balance sheet. As required by the new standards, these unrealized losses were reclassified to opening retained earnings.

Also prior to the adoption of these new standards, the unrealized gains associated with discontinued hedges were included in derivative instruments liability in the balance sheet. These gains were recognized in net income on the same basis as the net income recognition of the related hedged item. Consistent with the requirements of the new standards, these unrealized gains were reclassified to accumulated other comprehensive income as a cumulative opening adjustment.

**(Unaudited, in millions of dollars)**

## 4. Changes in accounting policies (continued):

On January 1, 2007, the Company made the following adjustments to the balance sheet to adopt the new standards:

| Balance sheet item | Increase (decrease) in $millions | Explanation |
|---|---|---|
| Future income tax asset – non-current | $ 22 | Cumulative prior period impacts of December 31, 2006 deferred unrealized losses relating to financial instruments not qualifying as hedges and cash flow hedges measured at fair value |
| Other assets | (15) | Deferred financing costs reclassified to long-term debt |
| Derivative instruments asset – non-current | (12) | Deferred unrealized losses relating to financial instruments not qualifying as hedges |
| Derivative instruments asset – current and non-current | 141 | Physical power and natural gas purchase and sales contracts measured at fair value |
| Derivative instruments asset – current and non-current | 91 | Cash flow hedges measured at fair value |
| Derivative instruments liability – current and non-current | 151 | Cash flow hedges measured at fair value |
| Derivative instruments liability – current and non-current | 45 | Physical power and natural gas purchase and sales contracts measured at fair value |
| Derivative instruments liability –non-current | (6) | Deferred unrealized gains relating to certain previously discontinued hedges reclassified to accumulated other comprehensive income |
| Long-term debt | (15) | Deferred financing costs reclassified from other assets |
| Future income tax liability – current and non-current | 11 | Cumulative prior period impacts of measuring natural gas supply contracts at fair value and of December 31, 2006 deferred unrealized gains on previously discontinued hedges. |
| Non-controlling interests | 70 | Cumulative prior period impacts of measuring natural gas supply contracts at fair value and of December 31, 2006 deferred unrealized gains on previously discontinued hedges. |
| Opening retained earnings | 20 | Cumulative prior period impact of measuring natural gas supply contracts at fair value (net of non-controlling interests of $66 million and income taxes of $10 million) |
| Opening retained earnings | (8) | Cumulative prior period impact of December 31, 2006 deferred unrealized losses relating to financial instruments not qualifying as hedges (net of income taxes of $4 million) |
| Opening accumulated other comprehensive loss | 42 | Cumulative prior period impact of cash flow hedges measured at fair value (net of income taxes of $18 million) |
| Opening accumulated other comprehensive loss | (1) | Cumulative prior period impact of December 31, 2006 deferred unrealized gains on previously discontinued hedges (net of non-controlling interests of $4 million and income taxes of $1 million) |

## 4. Changes in accounting policies (continued):

During the first quarter, the new accounting standards that require the fair value measurement of natural gas contracts and derivatives representing qualifying commodity hedges impacted the financial statements as follows:

| **Financial statement line item** | **Increase (decrease) $millions** |
|---|---|
| Derivative instruments asset – current and non-current | $ 38 |
| Future income tax asset | 11 |
| Derivative instruments liability – current and non-current | 26 |
| Future income tax liability | 5 |
| Non-controlling interests (balance sheet) | 31 |
| Revenues | 2 |
| Fuel expense | (44) |
| Income tax expense | 5 |
| Non-controlling interests (statement of income) | 31 |
| Accumulated other comprehensive loss | 23 |

### Future accounting changes

On December 1, 2006, the CICA issued new accounting standards for Capital Disclosures and Financial Instruments – Disclosures and Presentation. Effective January 1, 2008, the Company will adopt these new accounting standards.

As required by the new standards, the Company will disclose quantitative and qualitative information that is intended to provide users of the financial statements with additional disclosures on the Company's management of capital and on the risks associated with financial instruments. The Company is currently reviewing the impact of these new standards on its financial statements.

**(Unaudited, in millions of dollars)**

## 5. Financial instruments:

At March 31, 2007, the fair values of derivative instruments assets and liabilities are equal to their carrying values. The fair value of long-term debt, excluding capital lease obligations is $2,301 million compared to a carrying value of $2,038 million.

At December 31, 2006, the fair values of off-balance sheet contracts-for-differences were disclosed but were not included in the balance sheet.

The fair values of all other financial assets and financial liabilities including accounts receivable, short-term debt and accounts payable and accrued liabilities are not materially different from their carrying values due to their short-term nature.

Fair values of financial instruments are based on quoted market prices when these instruments are traded in active markets. In illiquid or inactive markets, EPCOR uses appropriate price modeling to estimate fair value.

The Company uses purchase and sales agreements including contracts-for-differences and foreign exchange contracts to hedge the variability in future cash flows. When the requirements are met and the derivative is highly effective, we use hedge accounting for offsetting the changes in cash flows attributable to the hedged risk.

## 6. Sale of power syndicate agreement:

During the current quarter, 10% of the Battle River Power Syndicate Agreement (Battle River PSA) was sold. This transaction was incremental to the initial sale of 55% of the Battle River PSA that was reported during the prior year. The current period's transaction is summarized as follows:

| | | |
|---|---|---|
| Cash proceeds from sale | $ | 59 |
| Less net book value and costs of disposal | | 25 |
| Gain on sale before income taxes | | 34 |
| Less future income taxes | | 4 |
| Gain on sale after income taxes | $ | 30 |

**(Unaudited, in millions of dollars)**

## 7. Income taxes and amounts in lieu of income taxes:

Income taxes and amounts in lieu of income taxes consisted of:

| Three months ended | March 31, 2007 | March 31, 2006 |
|---|---|---|
| Income taxes and amounts in lieu of income taxes on income from continuing operations for the quarter | $ 10 | $ 22 |
| Reduction of income taxes resulting from corporate restructuring within the Energy Services segment | (11) | - |
| Reduction of income taxes resulting from corporate restructuring within the Generation segment | - | (117) |
| | $ (1) | $ (95) |

### Corporate restructuring

On January 1, 2007, the Company reorganized certain subsidiaries within its Energy Services segment. As a result of the reorganization, the Company recognized future income tax assets of $11 million and a corresponding increase in consolidated net income in the first quarter of 2007. The resulting future income tax assets will be reduced over time, as the underlying income tax deductions are utilized to reduce taxable income.

On January 3, 2006, the Company announced that it reorganized certain subsidiaries within its Generation segment. As a result of the reorganization, the Company recognized an increase in non-current future income tax assets in the Company's consolidated balance sheet, with a corresponding income statement reduction of income taxes of $117 million.

**(Unaudited, in millions of dollars)**

## 8. Non-controlling interests:

Results of operations which relate to non-controlling interests are as follows:

| | Three months ended March 31 2007 | | Three months ended March 31 2006 | |
|---|---|---|---|---|
| Non-controlling interests in Power LP | $ | 49 | $ | 24 |
| Preferred share dividends paid by subsidiary companies | | 3 | | 5 |
| | $ | 52 | $ | 29 |

Non-controlling interests reflected in the consolidated balance sheets consisted of:

| | March 31, 2007 | | December 31, 2006 | |
|---|---|---|---|---|
| Non-controlling interests in Power LP, beginning of year | $ | 554 | $ | 542 |
| Partnership units issued to non-controlling interests | | - | | 55 |
| Earnings attributable to non-controlling interests | | 49 | | 43 |
| Other comprehensive income attributable to non-controlling interests | | 3 | | - |
| Opening retained earnings adjustment on implementation of financial instruments standards attributable to non-controlling interests | | 67 | | - |
| Distributions to non-controlling interests | | (22) | | (86) |
| Non-controlling interests in Power LP, end of period | | 651 | | 554 |
| Preferred shares issued by subsidiary companies, beginning of year | | 197 | | 346 |
| Redemption of preferred shares | | - | | (149) |
| Preferred shares issued by subsidiary companies, end of period | | 197 | | 197 |
| | $ | 848 | $ | 751 |

## 9. Guarantees:

The Company has issued letters of credit for $293 million (December 31, 2006 $248 million) to meet the credit requirements of energy market participants, to meet conditions of certain debt and service agreements, and to satisfy legislated reclamation requirements.

## 10. Segment disclosures:

The Company operates in the following reportable business segments, which follow the organization, management and reporting structure within the Company.

### Generation

Generation is involved in the development and operation of rate-regulated and non-rate-regulated electrical generation plants within Alberta, British Columbia, Ontario, and in the United States in Washington, Colorado, New York, New Jersey, California and North Carolina.

### Distribution and Transmission

Distribution and Transmission is involved in the transmission and distribution of electricity within The City of Edmonton.

### Energy Services

Energy Services is involved in the procurement, marketing and sale of electricity and natural gas in retail and wholesale markets in Alberta and Ontario.

### Water Services

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

### Corporate

Corporate reflects the costs of the Company's net unallocated corporate office expenses and net financing income earned from intercompany guarantee fees and intercompany interest charges.

(Unaudited, in millions of dollars)

## 10. Segment disclosures (continued):

**Three months ended March 31, 2007**

| | Generation | Distribution and Transmission | Energy Services | Water Services | Corporate | Intersegment Eliminations | Consolidated |
|---|---|---|---|---|---|---|---|
| Revenues – external | $ 217 | $ 28 | $ 610 | $ 43 | $ 1 | $ - | $ 899 |
| Intersegment revenues | 27 | 31 | 6 | - | - | (64) | - |
| Total revenues | 244 | 59 | 616 | 43 | 1 | (64) | 899 |
| Energy purchases and fuel | 27 | 16 | 578 | - | - | (56) | 565 |
| Operations, maintenance, administration and foreign exchange gain | 37 | 14 | 19 | 26 | 11 | (8) | 99 |
| Franchise fee, property taxes and other taxes | 5 | 9 | - | 2 | - | - | 16 |
| Depreciation, amortization and asset retirement accretion | 41 | 7 | 7 | 5 | 3 | - | 63 |
| Operating expenses | 110 | 46 | 604 | 33 | 14 | (64) | 743 |
| Operating income (loss) before corporate charges | 134 | 13 | 12 | 10 | (13) | - | 156 |
| Corporate charges | 7 | 2 | 3 | 2 | (14) | - | - |
| Operating income | $ 127 | $ 11 | $ 9 | $ 8 | $ 1 | $ - | $ 156 |
| Capital additions | $ 42 | $ 12 | $ 3 | $ 14 | $ 3 | $ - | $ 74 |

**Three months ended March 31, 2006**

| | Generation | Distribution and Transmission | Energy Services | Water Services | Corporate | Intersegment Eliminations | Consolidated |
|---|---|---|---|---|---|---|---|
| Revenues – external | $ 175 | $ 27 | $ 567 | $ 43 | $ - | $ - | $ 812 |
| Intersegment revenues | 27 | 34 | 5 | - | - | (66) | - |
| Total revenues | 202 | 61 | 572 | 43 | - | (66) | 812 |
| Energy purchases and fuel | 25 | 19 | 505 | - | - | (59) | 490 |
| Operations, maintenance, administration and foreign exchange gain | 31 | 13 | 19 | 26 | 8 | (7) | 90 |
| Franchise fee, property taxes and other taxes | 4 | 10 | - | 2 | - | - | 16 |
| Depreciation, amortization and asset retirement accretion | 37 | 7 | 7 | 4 | 3 | - | 58 |
| Operating expenses | 97 | 49 | 531 | 32 | 11 | (66) | 654 |
| Operating income (loss) before corporate charges | 105 | 12 | 41 | 11 | (11) | - | 158 |
| Corporate charges | 1 | 3 | 5 | 2 | (11) | - | - |
| Operating income | $ 104 | $ 9 | $ 36 | $ 9 | $ - | $ - | $ 158 |
| Capital additions | $ 13 | $ 11 | $ 1 | $ 11 | $ 2 | $ - | $ 38 |

**(Unaudited, in millions of dollars)**

## 10. Segment disclosures (continued):

### Geographic information:

| | Three months ended March 31, 2007 | | | | Three months ended March 31, 2006 | | | |
|---|---|---|---|---|---|---|---|---|
| | Canada | US | Intersegment Eliminations | Total | Canada | US | Intersegment Eliminations | Total |
| Revenues - external | $ 792 | $ 107 | $ - | $ 899 | $ 766 | $ 46 | $ - | $ 812 |
| Intersegment revenues | 5 | 6 | (11) | - | 5 | 1 | (6) | - |
| Total revenues | $ 797 | $ 113 | $ (11) | $ 899 | $ 771 | $ 47 | $ (6) | $ 812 |

## 11. Comparative figures:

Certain of the comparative figures have been reclassified to conform with the current period’s presentation.