

CONSOLIDATED STATEMENTS OF INCOME (LOSS) (UNAUDITED)

Three Months Ended March 31

(millions of dollars except where noted)

	2006	2005
Revenue		
Revenue before revenue limit and Market Power Mitigation Agreement rebates	1,568	1,770
Revenue limit rebate (Note 15)	(60)	-
Market Power Mitigation Agreement rebate	-	(412)
	1,508	1,358
Fuel expense	278	310
Gross margin	1,230	1,048
Expenses		
Operations, maintenance and administration	650	587
Depreciation and amortization (Note 4)	176	193
Accretion on fixed asset removal and nuclear waste management liabilities	125	119
Earnings on nuclear fixed asset removal and nuclear waste management funds	(89)	(71)
Property and capital taxes	25	21
	887	849
Income before the following:	343	199
Impairment of long-lived assets (Note 4)	-	202
Income (loss) before interest and income taxes	343	(3)
Net interest expense	49	47
Income (loss) before income taxes	294	(50)
Income tax expenses (recoveries)		
Current	20	7
Future (Note 9)	75	(19)
	95	(12)
Net income (loss)	199	(38)
Basic and diluted income (loss) per common share (dollars)	0.78	(0.15)
Common shares outstanding (millions)	256.3	256.3

See accompanying notes to the interim consolidated financial statements

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS (DEFICIT) (UNAUDITED)

Three Months Ended March 31

(millions of dollars)

	<u>2006</u>	<u>2005</u>
Retained earnings (deficit), beginning of period	261	(105)
Net income (loss)	<u>199</u>	<u>(38)</u>
Retained earnings (deficit), end of period	<u>460</u>	<u>(143)</u>

See accompanying notes to the interim consolidated financial statements

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

Three Months Ended March 31

(millions of dollars)

	2006	2005
Operating activities		
Net income (loss)	199	(38)
Adjust for non-cash items:		
Depreciation and amortization	176	193
Accretion on fixed asset removal and nuclear waste management liabilities	125	119
Earnings on nuclear fixed asset removal and nuclear waste management funds	(89)	(71)
Pension cost	54	28
Other post employment benefits and supplementary pension plans	64	45
Future income taxes	75	(19)
Transition rate option contracts	(9)	(9)
Mark-to-market on energy contracts	(9)	2
Provision for used nuclear fuel	8	7
Impairment of long-lived assets	-	202
Regulatory assets and liabilities	7	-
Other	-	(1)
	601	458
Contributions to nuclear fixed asset removal and nuclear waste management funds	(114)	(114)
Expenditures on fixed asset removal and nuclear waste management	(28)	(14)
Reimbursement of expenditures on nuclear fixed asset removal and nuclear waste management	7	6
Contributions to pension fund	(65)	(39)
Expenditures on other post employment benefits and supplementary pension plans	(15)	(16)
Expenditures on restructuring (Note 13)	(5)	(5)
Net changes to other long-term assets and liabilities	(31)	(9)
Changes in non-cash working capital balances (Note 17)	84	33
Cash flow provided by operating activities	434	300
Investing activities		
Investment in regulatory assets (Note 5)	(10)	(101)
Investment in fixed assets	(114)	(133)
Net proceeds from sale (purchase) of long term investments	2	(1)
Cash flow (used in) investing activities	(122)	(235)
Financing activities		
Issuance of long-term debt (Note 7)	-	95
Repayment of long-term debt (Note 7)	(301)	(1)
Net increase (decrease) in short-term notes (Note 6)	-	(26)
Cash flow (used in) provided by financing activities	(301)	68
Net increase in cash and cash equivalents	11	133
Cash and cash equivalents, beginning of period	908	2
Cash and cash equivalents, end of period	919	135

See accompanying notes to the interim consolidated financial statements

CONSOLIDATED BALANCE SHEETS (UNAUDITED)

As at <i>(millions of dollars)</i>	March 31	December 31
	2006	2005
Assets		
Current assets		
Cash and cash equivalents	919	908
Accounts receivable <i>(Note 3)</i>	339	538
Future income taxes	18	18
Fuel inventory	570	581
Materials and supplies	110	115
	1,956	2,160
Fixed assets <i>(Note 4)</i>		
Property, plant and equipment	15,278	15,172
Less: accumulated depreciation	3,927	3,760
	11,351	11,412
Other long-term assets		
Deferred pension asset	674	663
Nuclear fixed asset removal and nuclear waste management funds <i>(Note 8)</i>	6,984	6,788
Long-term materials and supplies	290	273
Regulatory assets <i>(Note 5)</i>	270	266
Long-term accounts receivable and other assets	58	61
	8,276	8,051
	21,583	21,623

See accompanying notes to the interim consolidated financial statements

CONSOLIDATED BALANCE SHEETS (UNAUDITED)

As at <i>(millions of dollars)</i>	March 31 2006	December 31 2005
Liabilities		
Current liabilities		
Accounts payable and accrued charges <i>(Notes 13 and 14)</i>	727	958
Revenue limit rebate payable <i>(Note 15)</i>	799	739
Long-term debt due within one year <i>(Note 7)</i>	706	806
Deferred revenue due within one year	12	12
Income and capital taxes payable	96	81
	<u>2,340</u>	<u>2,596</u>
Long-term debt <i>(Note 7)</i>	<u>2,888</u>	<u>3,089</u>
Other long-term liabilities		
Fixed asset removal and nuclear waste management <i>(Note 8)</i>	8,865	8,759
Other post employment benefits and supplementary pension plans	1,261	1,212
Long-term accounts payable and accrued charges	173	183
Deferred revenue	141	144
Future income taxes	316	241
Regulatory liabilities <i>(Note 5)</i>	13	12
	<u>10,769</u>	<u>10,551</u>
Shareholder's equity		
Common shares	5,126	5,126
Retained earnings	460	261
	<u>5,586</u>	<u>5,387</u>
	<u>21,583</u>	<u>21,623</u>

Commitments and Contingencies (Notes 1, 4, 6, 11, and 12)

See accompanying notes to the interim consolidated financial statements

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE MONTHS ENDED MARCH 31, 2006 AND 2005 (UNAUDITED)

1. BASIS OF PRESENTATION

These interim consolidated financial statements were prepared following the same accounting policies and methods as in the most recent annual consolidated financial statements, except as discussed in Note 2 to these interim consolidated financial statements. These interim financial statements do not contain all the disclosures required by Canadian generally accepted accounting principles for annual financial statements. Accordingly, these interim consolidated financial statements should be read in conjunction with the most recently prepared annual consolidated financial statements for the year ended December 31, 2005.

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

Certain of the 2005 comparative amounts have been reclassified from financial statements previously presented to conform to the 2006 financial statement presentation.

The consolidated financial statements include the accounts of Ontario Power Generation Inc. ("OPG" or the "Company") and its subsidiaries. OPG accounts for its interests in jointly controlled entities using the proportionate consolidation method. All significant intercompany transactions have been eliminated on consolidation.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Rate Regulated Accounting

In December 2004, the *Electricity Restructuring Act, 2004* (Bill 100) received royal assent. A regulation made pursuant to that statute in February 2005 provides that OPG receive regulated prices beginning April 1, 2005, for most of OPG's baseload hydroelectric facilities and all of its nuclear facilities. This includes electricity generated by Sir Adam Beck 1, 2 and Pump generating stations, DeCew Falls 1 and 2, and R.H. Saunders hydroelectric facilities, and Pickering A and B, and Darlington nuclear generating stations.

OPG's regulated prices were determined by the Province based on total projected production and costs of operation, plus the cost of capital including an average five per cent return on equity. The initial prices took effect April 1, 2005, and are expected to remain in effect until at least March 31, 2008, at which time it is anticipated that the Ontario Energy Board ("OEB") will establish new regulated prices. If there are changes to the fundamental assumptions on which these regulated prices were developed, the Province may amend these initial prices.

The OEB is a self-funding Crown corporation. Its mandate and authority come from the *Ontario Energy Board Act, 1998*, the *Electricity Act, 1998*, and a number of other provincial statutes. The OEB is an independent, quasi-judicial tribunal that reports to the Legislature of the Province through the Minister of Energy. It regulates all market participants in the province's natural gas and electricity industries and carries out its regulatory functions through public hearings and other more informal processes such as consultations.

Accounting standards recognize that rate regulation can create economic benefits and obligations, which are reported in the consolidated financial statements as regulatory assets and liabilities. When the regulation provides assurance that incurred costs will be recovered in the future, then OPG may defer those costs and report them as a regulatory asset. If current recovery is provided for costs expected to be incurred in the future, then OPG reports a regulatory liability. Also, if the regulation provides for lesser or greater than planned revenue to be received or returned by OPG through future rates, then OPG recognizes and reports a regulatory asset or liability, respectively. The measurement of such regulatory assets and liabilities are subject to certain estimates and assumptions, including assumptions made in the interpretation of the regulation. See Note 5 and Note 9 to the unaudited consolidated interim financial statements for additional disclosures required under Rate Regulated Accounting.

Long-Term Portfolio Investments

Long-term portfolio investments, other than investments owned by the Company's wholly owned subsidiary OPG Ventures Inc. ("OPGV"), are stated at amortized cost and include the nuclear fixed asset removal and nuclear waste management funds. Gains and losses on long-term investments are recognized when investments are sold. When a decline in the value of investments occurs, which is considered to be other than temporary, a provision for loss is established.

Investments owned by OPGV are recorded at fair value, and changes to the fair value of the investments are included in revenue in the period in which the change occurs. The fair values of these investments are estimated based on readily available market information or using estimation techniques based on historical performance.

Changes in Accounting Policies and Estimates

Reportable Segments

Effective April 1, 2005, the output from most of OPG's baseload hydroelectric facilities and all of its nuclear facilities became rate regulated. OPG continues to receive the spot market price for the output from its remaining hydroelectric, fossil-fuelled and wind generating stations, subject to a revenue limit on the majority of this output. With the introduction of rate regulation, OPG revised its reportable business segments to separately reflect the regulated and unregulated aspects of its business. Since the second quarter of 2005, OPG reported its business segments as Regulated – Nuclear, Regulated – Hydroelectric, and Unregulated Generation. Commencing in the first quarter of 2006, OPG has separated the Unregulated Generation business segment into two reportable segments, identified as Unregulated – Fossil-Fuelled and Unregulated – Hydroelectric, as a result of changes in the management structure of these segments. Results for the comparative periods have been reclassified to reflect the revised disclosure.

Estimated Service Life of Pickering B Generating Station

Effective January 1, 2006, following the completion of a review of the life limiting components of the Pickering B nuclear generating station, OPG revised and extended, for the purpose of calculating depreciation, the estimated remaining service life of the Pickering B nuclear generating station to 2014 from 2009.

Future Accounting Changes

In 2005, the Canadian Institute of Chartered Accountants (“CICA”) issued three new accounting standards: Handbook Section 1530, Comprehensive Income; Handbook Section 3855, Financial Instruments – Recognition and Measurement; and Handbook Section 3865, Hedges. These standards apply to interim and annual financial statements relating to fiscal years beginning on or after October 1, 2006.

These standards will be effective for OPG beginning in 2007. The impact of implementing these new standards on OPG’s consolidated financial statements is not yet determinable as it will be dependent on outstanding positions and their fair values at the time of transition. The following provides further information on each of the three new accounting standards as they relate to OPG.

Comprehensive Income

As a result of adopting these standards, a new category, accumulated other comprehensive income, will be added to shareholders’ equity in the consolidated balance sheets. Major components for this category will include unrealized gains and losses on financial assets classified as available-for-sale, changes in the fair value of the effective portion of cash flow hedging instruments, and unrealized foreign currency translation amounts, net of hedging, arising from self-sustaining foreign operations. These amounts will be recorded in the statement of other comprehensive income until the criteria for recognition in the consolidated statement of income are met.

Financial Instruments – Recognition and Measurement

Under the new standard, for accounting purposes, financial assets will be classified as one of the following: held-to-maturity, loans and receivables, held-for-trading or available-for-sale, and financial liabilities will be classified as held-for-trading or other than held-for-trading. Financial assets and liabilities held-for-trading will be measured at fair value with gains and losses recognized in net income. Financial assets held-to-maturity, loans and receivables and financial liabilities other than those held-for-trading, will be measured at amortized cost. Available-for-sale instruments will be measured at fair value with unrealized gains and losses recognized in other comprehensive income. The standard also permits designation of any financial instrument as held-for-trading upon initial recognition. All derivatives, including embedded derivatives that must be separately accounted for, generally must be classified as held-for-trading and recorded at fair value in the consolidated balance sheets.

Hedges

This new standard specifies the criteria under which hedge accounting can be applied and how hedge accounting is to be executed for each of the permitted hedging strategies: fair value hedges, cash flow hedges and hedges of a foreign currency exposure of a net investment in a self-sustaining foreign operation. In a fair value hedging relationship, the carrying value of the hedged item is adjusted by gains or losses attributable to the hedged risk and recognized in net income. This change in fair value of the hedged item, to the extent that the hedging relationship is effective, is offset by changes in the fair value of the derivative. In a cash flow hedging relationship, the effective portion of the change in the fair value of the hedging derivative will be recognized in other comprehensive income. The ineffective portion will be recognized in net income. The amounts recognized in accumulated other comprehensive income will be reclassified to net income in the periods in which net income is affected by the variability in the cash flows of the hedged item. In hedging a foreign currency exposure of a net investment in a self-sustaining foreign operation, foreign exchange gains and losses on the hedging instruments will be recognized in other comprehensive income.

3. SALE OF ACCOUNTS RECEIVABLE

On October 1, 2003, the Company signed an agreement to sell an undivided co-ownership interest in its current and future accounts receivable (the "receivables") to an independent trust. The Company also retains an undivided co-ownership interest in the receivables sold to the trust. Under the agreement, OPG continues to service the receivables. The transfer provides the trust with ownership of a share of the payments generated by the receivables, computed on a monthly basis. The trust's recourse to the Company is generally limited to its income earned on the receivables. In December 2005, the Company extended this agreement to August 2009.

OPG reflected the initial transfer to the trust of the co-ownership interest, and subsequent transfers required by the revolving nature of the securitization, as sales in accordance with CICA Accounting Guideline 12, *Transfer of Receivables*. In accordance with this Guideline, the proceeds of each sale to the trust were deemed to be the cash received from the trust net of the undivided co-ownership interest retained by the Company. For the three months ended March 31, 2006, the Company has recognized pre-tax charges of \$3 million (three months ended March 31, 2005 – \$2 million) on such sales at an average cost of funds of 4.1 per cent (three months ended March 31, 2005 – 2.9 per cent). As at March 31, 2006, OPG had sold receivables of \$300 million (December 31, 2005 – \$300 million) from its total portfolio of \$497 million (December 31, 2005 – \$668 million).

4. FIXED ASSETS

Depreciation and amortization expense for the three months ended March 31, 2006 and 2005 consists of the following:

<i>(millions of dollars)</i>	March 31 2006	March 31 2005
Depreciation and amortization	175	192
Nuclear waste management costs	1	1
	176	193

Interest capitalized to construction in progress at 6.0 per cent (three months ended March 31, 2005 – 6.0 per cent) during the three months ended March 31, 2006 was \$4 million (three months ended March 31, 2005 – \$8 million).

Impairment of Long-Lived Assets

The accounting estimates related to asset impairment require significant management judgment to identify factors such as short and long-term forecasts for future sales prices, the supply of electricity in Ontario, inflation, fuel prices and station lives. The amount of the future cash flow that OPG will ultimately realize with respect to these assets could differ materially from the carrying values recorded in the consolidated financial statements.

Lennox Generating Station

As a result of the Government's "Request for Information/Request for Proposal for 2,500 MW of New Clean Generation and Demand Side Management Projects" released in September 2004 and the related contractual arrangements, future wholesale electricity market revenue is expected to be lower than previously anticipated. As a relatively high variable cost plant, the Lennox generating station will not be able to recover its fixed operating costs and its carrying value from the wholesale electricity market in the future. Given these factors, OPG had initiated discussions with the Province, with the expectation of entering into a contractual arrangement for the recovery of the annual fixed operating costs and the carrying value of the Lennox generating station. In March 2005, the Province advised OPG that it would not support an arrangement that would allow for the recovery of the carrying value of the Lennox

generating station. As a result, OPG recorded an impairment loss of \$202 million in the first quarter of 2005.

In March 2006, the OEB issued a decision approving a reliability must-run (“RMR”) contract between OPG and the Independent Electricity System Operator (“IESO”) for the Lennox generating station, for the period October 1, 2005 to September 30, 2006. Reliability must-run contracts are designed to ensure that generating stations remain available to maintain the reliability of the electricity system. In its decision, the OEB found it appropriate for OPG to recover the fixed and variable operating costs of the Lennox generating stations that are not recovered through market revenues. As a result of the decision, OPG recorded \$29 million in revenue during the first quarter of 2006, of which approximately \$13 million relates to the period October 1, 2005 to December 31, 2005. The RMR contract is a cost-based contract that provides for regular payments, which are subject to adjustments for actual costs.

5. REGULATORY ASSETS AND LIABILITIES

The change in the regulatory assets and liabilities for the three months ended March 31, 2006 is as follows:

<i>(millions of dollars)</i>	December 31 2005	Additions	Amortization	March 31 2006
Regulatory assets				
Pickering A return to service costs	261	10	(10)	261
Ancillary services revenue variance account	5	4	-	9
Total regulatory assets	266	14	(10)	270
Regulatory liabilities				
Hydroelectric production variance account	4	-	-	4
Other	8	1	-	9
Total regulatory liabilities	12	1	-	13

Pickering A Return to Service Costs

Effective January 1, 2005, in accordance with a regulation made under the *Electricity Restructuring Act, 2004*, OPG was required to establish a deferral account in connection with non-capital costs that are associated with the return to service of units at the Pickering A nuclear generating station. As a result, the change in accounting was prospectively adopted on January 1, 2005, with no retroactive adoption. As at March 31, 2006, the deferral account was \$261 million, consisting of non-capital costs of \$233 million relating to Unit 1, and \$19 million relating to Units 2 and 3, \$16 million of general return to service costs, and interest of \$7 million. The accumulated amortization as of March 31, 2006 was \$14 million.

As at December 31, 2005, the deferral account was \$261 million, consisting of non-capital costs of \$228 million relating to Unit 1, and \$19 million relating to Units 2 and 3, \$11 million of general return to service costs, and interest of \$7 million. The accumulated amortization as of December 31, 2005 was \$4 million.

Under the regulation, the OEB is directed to ensure that OPG recovers any balance in the deferral account on a straight-line basis over a period not to exceed 15 years.

Variance Accounts

Effective April 1, 2005, in accordance with a regulation made under the *Electricity Restructuring Act, 2004*, OPG was directed to establish variance accounts for costs incurred on or after April 1, 2005 that are associated with differences in hydroelectric production due to differences between forecast and actual water conditions, changes in nuclear electricity production due to unforeseen changes to the law or to unforeseen technological changes, changes to revenues assumed for ancillary revenues from the regulated facilities, acts of God (including severe weather events), and transmission outages and transmission restrictions. OPG recorded an asset during the three months ended March 31, 2006 of \$4 million, reflecting ancillary services revenue that was unfavourable compared to that forecasted for 2006. The OEB is directed by the regulation to ensure recovery to the extent that the OEB is satisfied that the costs recorded in the account were prudently incurred and accurately recorded. Any balances approved by the OEB will be amortized over a period not to exceed three years. The amortization will commence after OPG receives a rate order from the OEB.

The other regulatory liability consists of a portion of non-regulated revenue earned by OPG's regulated assets, which will result in a reduction of future regulated rates to be established by the OEB. OPG recorded an additional liability of \$1 million during the three months ended March 31, 2006.

Had OPG not accounted for the variances as a regulatory asset and liability, revenue for first quarter of 2006 would have been lower by \$3 million.

6. SHORT-TERM CREDIT FACILITIES

OPG's 364-day term \$1 billion revolving committed bank credit facility is divided into two tranches – a \$500 million 364-day term tranche maturing May 23, 2006, and a \$500 million three-year term tranche maturing May 23, 2008. OPG has received commitments from the banks to renew and extend the maturity dates to May 22, 2007 and May 22, 2009 for the respective tranches. The total credit facility will be used primarily as support for notes issued under OPG's commercial paper program. As of March 31, 2006, OPG had no commercial paper or other outstanding borrowing under this facility.

OPG also maintains \$26 million (December 31, 2005 – \$26 million) in short-term uncommitted overdraft facilities as well as \$215 million (December 31, 2005 – \$215 million) of short-term uncommitted credit facilities, which support the issuance of Letters of Credit. OPG uses Letters of Credit to support the supplementary pension plans and is required to post Letters of Credit as collateral with Local Distribution Companies ("LDCs") as prescribed by the OEB's Retail Settlement Code. At March 31, 2006, there was a total of \$143 million (December 31, 2005 – \$157 million) of Letters of Credit issued, which included \$138 million relating to the supplementary pension plans (December 31, 2005 – \$138 million) and \$5 million (December 31, 2005 – \$19 million) relating to collateral requirements to the LDCs.

7. LONG-TERM DEBT

Long-term debt consists of the following:

<i>(millions of dollars)</i>	March 31 2006	December 31 2005
Notes payable to the Ontario Electricity Financial Corporation	3,395	3,695
Share of non-recourse limited partnership debt	199	200
	3,594	3,895
Less: due within one year		
Notes payable to the Ontario Electricity Financial Corporation	700	800
Share of limited partnership debt	6	6
	706	806
Long-term debt	2,888	3,089

Holders of the senior debt are entitled to receive, in full, amounts owing in respect of the senior debt before holders of the subordinated debt are entitled to receive any payments. The Ontario Electricity Financial Corporation ("OEFC") currently holds all of OPG's outstanding senior and subordinated notes.

Interest paid during the three months ended March 31, 2006 was \$119 million (three months ended March 31, 2005 – \$103 million), of which \$114 million relates to interest paid on long-term debt (three months ended March 31, 2005 – \$100 million). Interest on the notes payable to OEFC is paid in the first and third quarter of the year.

8. FIXED ASSET REMOVAL AND NUCLEAR WASTE MANAGEMENT

The liability for fixed asset removal and nuclear waste management on a present value basis consists of the following:

<i>(millions of dollars)</i>	March 31 2006	December 31 2005
Liability for nuclear used fuel management	5,007	4,940
Liability for nuclear decommissioning and low and intermediate level waste management	3,665	3,627
Liability for non-nuclear fixed asset removal	193	192
Fixed asset removal and nuclear waste management liability	8,865	8,759

The change in the fixed asset removal and nuclear waste management liability for the three months ended March 31, 2006 and the year ended December 31, 2005 are as follows:

<i>(millions of dollars)</i>	March 31 2006	December 31 2005
Liability, beginning of period	8,759	8,339
Increase in liability due to accretion	125	476
Increase in liability due to nuclear used fuel and nuclear waste management variable expenses	9	34
Liabilities settled by expenditures on waste management	(28)	(90)
Liability, end of period	8,865	8,759

OPG recognizes asset retirement obligations for fixed asset removal and nuclear waste management, discounted for the time value of money. OPG has estimated both the amount and timing of future cash expenditures based on current plans for fixed asset removal and nuclear waste management. The liabilities are initially recorded at their estimated fair value, which is based on a discounted value of the expected costs to be paid.

Ontario Nuclear Funds Agreement

OPG sets aside and invests funds in segregated custodian accounts specifically for discharging its nuclear fixed asset removal and nuclear waste management liabilities. The nuclear fixed asset removal and nuclear waste management funds as at March 31, 2006 and December 31, 2005, consist of the following:

<i>(millions of dollars)</i>	Amortized Cost Basis		Fair Value	
	March 31 2006	December 31 2005	March 31 2006	December 31 2005
Decommissioning Fund	4,170	4,106	4,782	4,583
Due to Province – Decommissioning Fund	(16)	(7)	(628)	(484)
	4,154	4,099	4,154	4,099
Used Fuel Fund ¹	2,843	2,693	3,233	2,995
Due (to) from Province – Used Fuel Fund	(13)	(4)	(403)	(306)
	2,830	2,689	2,830	2,689
	6,984	6,788	6,984	6,788

¹ The Ontario NFWA Trust represents \$1,064 million as at March 31, 2006 (December 31, 2005 – \$1,003 million) of the Used Fuel Fund on an amortized cost basis.

9. INCOME TAXES

OPG follows the liability method of tax accounting for its unregulated operations. Under the liability method, future tax assets and liabilities are determined based on differences between the accounting and tax bases of assets and liabilities and measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse. The effect on future income tax assets and liabilities of a change in tax rates is included in income in the period the change is substantively enacted. Future income tax assets are evaluated and if realization is not considered more likely than not, a valuation allowance is established. Commencing April 1, 2005, with the introduction of rate regulation,

OPG accounts for income taxes relating to the rate regulated segments of its business using the taxes payable method. Under the taxes payable method, OPG does not recognize future income taxes relating to the rate regulated segments of its business to the extent those future income taxes are expected to be recovered in the regulated rates charged to future customers.

The following table summarizes the income statement and balance sheet amounts under the method used by the company to account for income taxes compared to what would have been reported had OPG applied the liability method for the regulated business for the three months ended March 31, 2006:

<i>(millions of dollars)</i>	As Stated	Liability Method
Future income tax expense	75	85
Current portion (assets)	(18)	(38)
Long-term portion (liability)	316	429

Had OPG continued to use the liability method for the regulated business, the future tax expense for the three months ended March 31, 2006 would have increased by \$10 million with a corresponding increase in the future income tax liability (year ended December 31, 2005 – \$157 million).

The amount of cash income taxes paid during the three months ended March 31, 2006 was \$8 million (three months ended March 31, 2005 – \$4 million).

10. BENEFIT PLANS

The post employment benefit programs include pension, group life insurance, health care and long-term disability benefits. Pension and other post employment benefit (“OPEB”) obligations are impacted by factors including interest rates, adjustments arising from plan amendments, changes in assumptions and experience gains or losses. The 2006 costs are based on a measurement of the pension and OPEB obligations and the pension fund assets, as at December 31, 2005.

Total benefit costs for the three months ended March 31, 2006 and 2005, are as follows:

<i>(millions of dollars)</i>	March 31 2006	March 31 2005
Registered pension plan	54	28
Supplementary pension plans	4	4
OPEB	60	41

11. FINANCIAL INSTRUMENTS

Fair values of derivative instruments have been estimated by reference to quoted market prices for actual or similar instruments where available. Where quoted market prices are not available, OPG considers various factors to estimate forward prices, including market prices and price volatility in neighbouring electricity markets, market prices for fuel, and other factors.

Trading activities and liquidity in the Ontario electricity market have been limited as companies are generally entering only into short-term contracts. As a result, forward pricing information for contracts may not accurately represent the cost to enter into these contracts. For Ontario-based contracts that are not entered into for hedging purposes, OPG established liquidity reserves against the fair market value of the assets and liabilities equal to the gain or loss on these contracts. These reserves decreased trading revenue by \$9 million during the three months ended March 31, 2006 (three months ended March 31, 2005 – increased by \$5 million). Contracts for transactions outside of Ontario continue to be carried on the consolidated balance sheets as assets or liabilities at fair value, with changes in fair value recorded in trading revenue as gains or losses.

Derivative Instruments Used for Hedging Purposes

The following table provides the estimated fair value of derivative instruments designated as hedges. The majority of OPG's derivative instruments are treated as hedges, with gains or losses recognized upon settlement when the underlying transactions occur. OPG holds financial commodity derivatives primarily to hedge the commodity price exposure associated with changes in the price of electricity.

<i>(millions of dollars except where noted)</i>	Notional Quantity	Terms	Fair Value	Notional Quantity	Terms	Fair Value
	March 31, 2006			December 31, 2005		
Gain (loss)						
Electricity derivative instruments	3.1 TWh	1-2 yrs	(54)	4.1 TWh	1-2 yrs	(125)
Foreign exchange derivative instruments	U.S. \$3	Apr/06	-	U.S. \$15	Jan/06	-
Interest rate hedges	400	1-15 yrs	2	400	1-15 yrs	(7)

Foreign exchange derivative instruments are used to hedge the exposure to anticipated U.S. dollar denominated purchases. The weighted average fixed exchange rate for contracts outstanding at March 31, 2006 was U.S. \$0.86 (December 31, 2005 – U.S. \$0.87) for every Canadian dollar.

OPG entered into a number of forward start interest rate swap agreements to hedge against the effect of future interest rate movement based on the anticipated future borrowing requirement for the Niagara tunnel project. These transactions are ordinarily accounted for as hedges, however, a gain of approximately \$3 million (year ended December 31, 2005 – loss of \$5 million) was recorded to account for ineffectiveness in the hedges.

Derivative Instruments Not Used for Hedging Purposes

The carrying amount (fair value) of derivative instruments not designated for hedging purposes is as follows:

<i>(millions of dollars except where noted)</i>	Notional Quantity	Fair Value	Notional Quantity	Fair Value
	March 31, 2006		December 31, 2005	
Foreign exchange derivative	-	-	U.S. \$3	-
Commodity derivative instruments				
Assets	5.8 TWh	19	3.3 TWh	13
Liabilities	1.5 TWh	(23)	1.1 TWh	(37)
		(4)		(24)
Ontario market liquidity reserve		(12)		(3)
Total		(16)		(27)

Foreign exchange derivative instruments that are not designated as hedges have a weighted average exchange rate of U.S. \$0.85 at December 31, 2005.

12. COMMITMENTS AND CONTINGENCIES

Litigation

Various legal proceedings are pending against OPG or its subsidiaries covering a wide range of matters that arise in the ordinary course of its business activities.

In July 2004, OPG and two individual OPG employees were each charged with criminal negligence causing death and criminal negligence causing bodily harm in relation to a 2002 drowning accident at Barrett Chute. The trial commenced on January 16, 2006, and is expected to last at least until the late fall of 2006. Also, certain First Nations have commenced actions for interference with reserve and traditional land rights. The claims by some of these First Nations total approximately \$50 million and claims by others are for unspecified amounts.

Each of these matters is subject to various uncertainties. Some of these matters may be resolved unfavourably with respect to OPG and could have a significant effect on OPG's financial position. Management has provided for contingencies that are determined to be likely and are reasonably measurable.

Environmental

OPG was required to assume certain environmental obligations from Ontario Hydro. A provision of \$76 million was established as at April 1, 1999 for such obligations. During the three months ended March 31, 2006, expenditures of \$1 million were recorded against the provision.

Current operations are subject to regulation with respect to air, soil and water quality and other environmental matters by federal, provincial and local authorities. The cost of obligations associated with current operations is provided for on an ongoing basis. Management believes it has made adequate provision in its consolidated financial statements to meet OPG's current environmental obligations.

Guarantees

As part of normal business, OPG and certain of its subsidiaries enter into various agreements providing financial or performance assurance to third parties on behalf of certain subsidiaries. Such agreements include guarantees, standby Letters of Credit and surety bonds.

13. RESTRUCTURING

The change in the restructuring liability for termination benefits for the three months ended March 31, 2006 and the year ended December 31, 2005 are as follows:

<i>(millions of dollars)</i>	March 31 2006	December 31 2005
Liability, beginning of period	12	20
Restructuring charges	-	10
Payments	(5)	(18)
Liability, end of period	7	12

During 2005, OPG recorded restructuring charges of \$10 million, which consisted of \$4 million related to the Lakeview generating station in the Unregulated – Fossil-Fuelled segment and \$6 million related to the Energy Markets business which was included in the Other segment. No additional restructuring charge was recorded during the first quarter of 2006.

14. TRANSITION RATE OPTION CONTRACTS

Under regulation known as Transition – Generation Corporation Designated Rate Options (“TRO”), OPG has been required to provide transitional price relief since market opening to certain power customers for up to four years based on the consumption and average price paid by each customer during a reference period of July 1, 1999 to June 30, 2000. The TRO is treated as a hedge of generation revenue. The maximum length of the program is four years, which expires April 30, 2006.

Provisions totalling \$240 million on the TRO contracts were recorded in 2002 and 2003 based on the estimated future losses on these contracts. The provisions were determined at that time using management’s best estimates of the forward price curve for electricity, wholesale electricity market fees, impact of decontrol on these contracts, interruptions of volume, and the recovery of Market Power Mitigation Agreement rebates.

The change in the TRO contracts provision for the three months ended March 31, 2006 and the year ended December 31, 2005 are as follows:

<i>(millions of dollars)</i>	March 31 2006	December 31 2005
Provision, beginning of period	12	48
Decrease of provision during the period	(9)	(36)
Provision, end of period	3	12

15. REVENUE LIMIT REBATE

Eighty-five per cent of the generation output from OPG’s unregulated generation assets, excluding the Lennox generating station, TRO volumes and forward sales as of January 1, 2005, is subject to a revenue limit based on an average price of \$47.00/MWh (4.7¢/kWh). This revenue limit was originally established for a period of 13 months ending April 30, 2006, which was subsequently extended for an additional three years. Starting May 1, 2006, the revenue limit decreased to 4.6¢/kWh from the previous limit of 4.7¢/kWh. On May 1, 2007, the revenue limit will return to 4.7¢/kWh and increase to 4.8¢/kWh effective May 1, 2008. In addition, volumes sold under a Pilot Auction administered by the Ontario Power Authority will receive a revenue limit that is 0.5¢/kWh higher than the revenue limit applicable to OPG’s other generating assets. Revenues above these limits will be returned to the IESO for the benefit of consumers.

The change in the revenue limit rebate liability for the three months ended March 31, 2006 and the year ended December 31, 2005 are as follows:

<i>(millions of dollars)</i>	March 31 2006	December 31 2005
Liability, beginning of period	739	-
Increase to provision during the period	60	739
Liability, end of period	799	739

16. BUSINESS SEGMENTS

Effective April 1, 2005, the output from most of OPG’s baseload hydroelectric facilities and all of its nuclear facilities became rate regulated. With the introduction of rate regulation, OPG revised its reportable business segments to separately reflect the regulated and unregulated aspects of its business. Commencing in the first quarter of 2006, OPG has separated the Unregulated Generation business

segment into two reportable segments identified as Unregulated – Fossil-Fuelled and Unregulated – Hydroelectric, as a result of changes in the management structure of these segments. Results for the comparative periods have been reclassified to reflect the revised disclosure.

Segment Income for Three Months Ended March 31, 2006 <i>(millions of dollars)</i>	Regulated		Unregulated			Total
	Nuclear	Hydro-electric	Hydro-electric	Fossil-Fuelled	Other	
Revenues						
Revenue	709	175	224	421	39	1,568
Revenue limit rebate	-	-	(20)	(40)	-	(60)
	709	175	204	381	39	1,508
Fuel expense	31	52	20	175	-	278
Gross margin	678	123	184	206	39	1,230
Operations, maintenance and administration	471	21	36	115	7	650
Depreciation and amortization	89	16	16	51	4	176
Accretion on fixed asset removal and nuclear waste management liabilities	123	-	-	2	-	125
Earnings on nuclear fixed asset removal and nuclear waste management funds	(89)	-	-	-	-	(89)
Property and capital taxes	10	5	4	4	2	25
Income before interest and income taxes	74	81	128	34	26	343

Segment (Loss) Income for Three Months Ended March 31, 2005 <i>(millions of dollars)</i>	Regulated		Unregulated			Total
	Nuclear	Hydro-electric	Hydro-electric	Fossil-Fuelled	Other	
Revenues						
Revenue	740	270	231	510	19	1,770
Market Power Mitigation Agreement rebate	(160)	(65)	(58)	(129)	-	(412)
	580	205	173	381	19	1,358
Fuel expense	29	53	19	209	-	310
Gross margin	551	152	154	172	19	1,048
Operations, maintenance and administration	418	18	29	108	14	587
Depreciation and amortization	92	18	16	58	9	193
Accretion on fixed asset removal and nuclear waste management liabilities	117	-	-	2	-	119
Earnings on nuclear fixed asset removal and nuclear waste management funds	(71)	-	-	-	-	(71)
Property and capital taxes	11	4	3	5	(2)	21
(Loss) income before the following:	(16)	112	106	(1)	(2)	199
Impairment of long-lived assets	-	-	-	202	-	202
(Loss) income before interest and income taxes	(16)	112	106	(203)	(2)	(3)

	Regulated		Unregulated			Total
	Nuclear	Hydro-electric	Hydro-electric	Fossil-Fuelled	Other	
<i>(millions of dollars)</i>						
Selected Balance Sheet Information						
March 31, 2006						
Segment property, plant and equipment, net	3,113	4,072	3,073	498	595	11,351
December 31, 2005						
Segment property, plant and equipment, net	3,156	4,054	3,076	531	595	11,412
Selected Cash Flow Information						
March 31, 2006						
Capital expenditures	41	34	11	14	14	114
March 31, 2005						
Capital expenditures	95	17	7	10	4	133

17. CHANGES IN NON-CASH WORKING CAPITAL BALANCES

<i>(millions of dollars)</i>	Three Months Ended March 31	
	2006	2005
Accounts receivable	197	(89)
Fuel inventory	11	99
Materials and supplies	5	(14)
Market Power Mitigation Agreement rebate payable	-	192
Revenue limit rebate payable	60	-
Accounts payable and accrued charges	(204)	(163)
Income and capital taxes payable	15	8
	84	33

18. SEASONAL OPERATIONS

OPG's quarterly results are impacted by changes in demand resulting from variations in seasonal weather conditions. Historically, OPG's revenues are higher in the first and third quarters of a fiscal year as a result of winter heating demands in the first quarter and air conditioning/cooling demands in the third quarter. Regulated prices for the baseload hydroelectric and nuclear facilities, the revenue limit related to the generation from OPG's other generating assets and OPG's hedging strategies significantly reduced the impact of seasonal price fluctuations on the results of operations.