

## INTERIM CONSOLIDATED STATEMENTS OF (LOSS) INCOME (UNAUDITED)

	Three Months Ended		Nine Months Ended	
	September 30 2008	2007	September 30 2008	2007
<i>(millions of dollars except where noted)</i>				
<b>Revenue</b> (Note 16)				
Revenue before revenue limit rebate	1,628	1,481	4,698	4,494
Revenue limit rebate (Note 15)	(115)	(60)	(237)	(176)
	<b>1,513</b>	1,421	<b>4,461</b>	4,318
Fuel expense (Note 16)	334	336	915	962
<b>Gross margin</b> (Note 16)	<b>1,179</b>	1,085	<b>3,546</b>	3,356
<b>Expenses</b>				
Operations, maintenance and administration	689	689	2,130	2,159
Depreciation and amortization (Note 5)	162	168	497	519
Accretion on fixed asset removal and nuclear waste management liabilities (Note 9)	151	127	438	381
Losses (earnings) on nuclear fixed asset removal and nuclear waste management funds (Note 9)	190	(92)	133	(392)
Property and capital taxes	24	17	54	66
	<b>1,216</b>	909	<b>3,252</b>	2,733
<b>(Loss) income before the following:</b>	<b>(37)</b>	176	<b>294</b>	623
Other losses (Notes 3 and 16)	-	-	7	-
<b>(Loss) income before interest and income taxes</b>	<b>(37)</b>	176	<b>287</b>	623
Net interest expense (Note 8)	41	37	120	102
<b>(Loss) income before income taxes</b>	<b>(78)</b>	139	<b>167</b>	521
Income tax expense (Note 10)				
Current	33	21	179	98
Future	31	5	(131)	14
	<b>64</b>	26	<b>48</b>	112
<b>Net (loss) income</b>	<b>(142)</b>	113	<b>119</b>	409
<b>Basic and diluted (loss) income per common share</b> (dollars)	<b>(0.55)</b>	0.44	<b>0.46</b>	1.60
<b>Common shares outstanding</b> (millions)	<b>256.3</b>	256.3	<b>256.3</b>	256.3

See accompanying notes to the interim consolidated financial statements

## INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

<i>(millions of dollars)</i>	Three Months Ended September 30		Nine Months Ended September 30	
	2008	2007	2008	2007
<b>Operating activities</b>				
Net (loss) income	(142)	113	119	409
Adjust for non-cash items:				
Depreciation and amortization <i>(Note 5)</i>	162	168	497	519
Accretion on fixed asset removal and nuclear waste management liabilities <i>(Note 9)</i>	151	127	438	381
Losses (earnings) on nuclear fixed asset removal and nuclear waste management funds	190	(92)	133	(392)
Pension and other post employment benefit costs <i>(Note 11)</i>	103	125	315	368
Future income taxes <i>(Note 10)</i>	31	5	(131)	14
Other	(19)	15	30	79
	<b>476</b>	461	<b>1,401</b>	1,378
Contributions to nuclear fixed asset removal and nuclear waste management funds	(113)	(113)	(340)	(340)
Expenditures on nuclear fixed asset removal and nuclear waste management	(40)	(48)	(135)	(148)
Reimbursement of expenditures on nuclear fixed asset removal and nuclear waste management	46	16	54	102
Contributions to Pension Fund	(66)	(66)	(198)	(198)
Expenditures on other post employment benefits and supplementary pension plans	(21)	(19)	(60)	(53)
Revenue limit rebate <i>(Note 15)</i>	(93)	(101)	(189)	(149)
Expenditure on restructuring	-	-	-	(2)
Net changes to other long-term assets and liabilities	(13)	(18)	119	(37)
Changes in non-cash working capital balances <i>(Note 17)</i>	258	136	183	170
<b>Cash flow provided by operating activities</b>	<b>434</b>	248	<b>835</b>	723
<b>Investing activities</b>				
Decrease in regulatory assets <i>(Note 6)</i>	(2)	(10)	(12)	(48)
Investment in fixed assets	(172)	(179)	(434)	(476)
Net proceeds from sale of long-term assets	9	-	15	-
Cash and cash equivalent transferred to short-term investments	1	(103)	-	(103)
<b>Cash flow used in investing activities</b>	<b>(164)</b>	(292)	<b>(431)</b>	(627)
<b>Financing activities</b>				
Issuance of long-term debt <i>(Note 7)</i>	50	240	375	450
Repayment of long-term debt <i>(Note 7)</i>	(202)	(202)	(406)	(405)
Net decrease in short-term notes	-	-	-	(15)
<b>Cash flow provided by (used in) financing activities</b>	<b>(152)</b>	38	<b>(31)</b>	30
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>118</b>	(6)	<b>373</b>	126
<b>Cash and cash equivalents, beginning of period</b>	<b>365</b>	138	<b>110</b>	6
<b>Cash and cash equivalents, end of period</b>	<b>483</b>	132	<b>483</b>	132

See accompanying notes to the interim consolidated financial statements

## INTERIM CONSOLIDATED BALANCE SHEETS (UNAUDITED)

As at (millions of dollars)	September 30 2008	December 31 2007
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	483	110
Accounts receivable (Note 4)	227	315
Fuel inventory	580	604
Prepaid expenses	39	35
Future income taxes (Note 10)	5	12
Materials and supplies (Note 2)	128	125
	<u>1,462</u>	<u>1,201</u>
<b>Fixed assets (Notes 2 and 16)</b>		
Property, plant and equipment	18,134	17,772
Less: accumulated depreciation	5,390	4,995
	<u>12,744</u>	<u>12,777</u>
<b>Other long-term assets</b>		
Deferred pension asset	788	731
Nuclear fixed asset removal and nuclear waste management funds (Note 9)	9,416	9,263
Long-term investments (Note 3)	82	93
Long-term materials and supplies	342	353
Future income taxes (Note 10)	24	-
Regulatory assets (Note 6)	370	356
Long-term accounts receivable and other assets	47	65
	<u>11,069</u>	<u>10,861</u>
	<u>25,275</u>	<u>24,839</u>

See accompanying notes to the interim consolidated financial statements

## INTERIM CONSOLIDATED BALANCE SHEETS (UNAUDITED)

As at (millions of dollars)	September 30 2008	December 31 2007
<b>Liabilities</b>		
<b>Current liabilities</b>		
Accounts payable and accrued charges	794	953
Revenue limit rebate payable (Note 15)	148	100
Long-term debt due within one year (Note 7)	357	407
Deferred revenue due within one year	12	12
Income and capital taxes payable	59	66
	<u>1,370</u>	<u>1,538</u>
<b>Long-term debt (Note 7)</b>	<u>3,465</u>	<u>3,446</u>
<b>Other long-term liabilities</b>		
Fixed asset removal and nuclear waste management (Note 9)	11,313	10,957
Other post employment benefits and supplementary pension plans	1,670	1,556
Long-term accounts payable and accrued charges	433	184
Deferred revenue	112	120
Future income taxes (Note 10)	-	217
Regulatory liabilities (Note 6)	13	14
	<u>13,541</u>	<u>13,048</u>
<b>Shareholder's equity</b>		
Common shares	5,126	5,126
Retained earnings	1,783	1,664
Accumulated other comprehensive (loss) income	(10)	17
	<u>6,899</u>	<u>6,807</u>
	<u>25,275</u>	<u>24,839</u>

Commitments and Contingencies (Notes 3, 6, 7, 12, and 14)

See accompanying notes to the interim consolidated financial statements

**INTERIM CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDER'S EQUITY  
(UNAUDITED)**

<i>(millions of dollars)</i>	<b>Nine Months Ended September 30</b>	
	<b>2008</b>	<b>2007</b>
<b>Common shares</b>	<b>5,126</b>	5,126
<b>Retained earnings</b>		
Balance at beginning of period	<b>1,664</b>	623
Transition adjustment on adoption of financial instruments accounting standards	-	513
Net income	<b>119</b>	409
Balance at end of period	<b>1,783</b>	1,545
<b>Accumulated other comprehensive (loss) income, net of income taxes</b>		
Balance at beginning of period	<b>17</b>	-
Transition adjustment on adoption of financial instruments accounting standards <i>(Note 2)</i>	-	21
Other comprehensive (loss) income for the period	<b>(27)</b>	11
Balance at end of period	<b>(10)</b>	32
<b>Total shareholder's equity at end of period</b>	<b>6,899</b>	6,703

**INTERIM CONSOLIDATED STATEMENT OF COMPREHENSIVE (LOSS) INCOME  
(UNAUDITED)**

<i>(millions of dollars)</i>	<b>Three Months Ended September 30 2008</b>	<b>Nine Months Ended September 30 2008</b>
	<b>Net (loss) income</b>	<b>(142)</b>
<b>Other comprehensive (loss) income, net of income taxes</b>		
Net (loss) on derivatives designated as cash flow hedges <sup>1</sup>	<b>10</b>	<b>(20)</b>
Reclassification to income of gains on derivatives designated as cash flow hedges <sup>2</sup>	<b>(3)</b>	<b>(7)</b>
Other comprehensive income (loss) for the period	<b>7</b>	<b>(27)</b>
<b>Comprehensive (loss) income</b>	<b>(135)</b>	<b>92</b>

<sup>1</sup> Net of income tax recoveries of \$5 million and \$2 million for the three and nine months ended September 30, 2008, respectively.

<sup>2</sup> Net of income tax expenses of \$2 million and \$5 million for the three and nine months ended September 30, 2008, respectively.

*See accompanying notes to the interim consolidated financial statements*

## **NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2008 AND 2007 (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 consolidated 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, 2007.

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, revenue and expenses, and the disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

Certain of the 2007 comparative amounts have been reclassified from financial statements previously presented to conform to the 2008 financial statement presentation.

The interim 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**

A regulation pursuant to the *Electricity Restructuring Act, 2004* (Ontario), provides that, effective April 1, 2005, OPG receives regulated prices for electricity generated from most of its baseload hydroelectric facilities and all of the nuclear facilities that it operates. This includes electricity generated from 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 facilities.

In November 2007, OPG filed an application with the Ontario Energy Board ("OEB") for new payment amounts for its regulated facilities effective April 1, 2008, for a 21-month period. In February 2008, the OEB granted OPG's request that payment amounts for its regulated facilities be declared interim effective April 1, 2008, until such time that final payment amounts would be approved by the OEB.

A hearing on OPG's application for new payment amounts was completed on August 5, 2008. The OEB's decision on the application was issued on November 3, 2008. The OEB has not determined OPG's new payment amounts as of the date of these statements. On November 13, 2008, OPG filed a draft rate order with the OEB to reflect adjustments to the proposed revenue requirement and payment amounts. The OEB is expected to finalize OPG's payment amounts before the end of November 2008.

In its decision, the OEB determined that the new payment amounts should apply retrospectively starting on April 1, 2008. The OEB also directed that the payment amounts are to be adjusted through the use of a rate rider on production to allow for recovery of the approved 21-month revenue requirement over the 13-month period from December 1, 2008 to December 31, 2009. The retrospective revenue will be equal to the difference between the new payment amounts approved by the OEB and the existing payment amounts, multiplied by OPG's monthly forecast production for the period April 1, 2008 to November 30,

2008 included in the original application to the OEB. OPG will record the impact of the retrospective increase in the payment amounts to April 1, 2008, during the fourth quarter of 2008.

The OEB also approved a revised incentive mechanism to optimize hydroelectric production based on market signals. This new mechanism will apply to the period after December 1, 2008. Under this mechanism, OPG will receive the approved hydroelectric payment amount for the average hourly net energy production from the prescribed hydroelectric facilities in that month. Net energy production in any hour that is over the average hourly volume will receive the market price. In hours when the net energy production is less than the average hourly volume, OPG's revenues will be adjusted by the difference between the average hourly volume and the actual net energy production times the market price.

Accounting standards recognize that rate regulation can create economic benefits and obligations, which are reported in the unaudited interim consolidated financial statements as regulatory assets and liabilities. Where rate regulation provides assurance that incurred expenses will be recovered in the future, then OPG may defer those expenses and report them as a regulatory asset. If current recovery is provided for expenses 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 regulated prices, then OPG recognizes and reports a regulatory asset or liability, respectively. The measurement of regulatory assets and liabilities is subject to certain estimates and assumptions, including assumptions made in the interpretation of the regulation. See Notes 6 and 10 to the unaudited interim consolidated financial statements for additional disclosure related to rate regulated accounting.

## **Changes in Accounting Policies and Estimates**

### *Financial Instruments and Capital Disclosures – Disclosure and Presentation*

On January 1, 2008, OPG adopted three new presentation and disclosure standards that were issued by the Canadian Institute of Chartered Accountants ("CICA"): Handbook Section 3862, *Financial Instruments – Disclosures*, Handbook Section 3863, *Financial Instruments – Presentation*, and Handbook Section 1535, *Capital Disclosures*.

Handbook Section 3862, *Financial Instruments – Disclosures*, outlines disclosure requirements for financial instruments and places increased emphasis on disclosure about the risks associated with recognized and unrecognized financial instruments and how these risks are managed.

Handbook Section 3863, *Financial Instruments – Presentation*, carries forward the presentation requirements from Section 3861, *Financial Instruments – Disclosure and Presentation*.

Handbook Section 1535, *Capital Disclosures*, requires the disclosure of both qualitative and quantitative information that enables users of financial statements to evaluate a company's objectives, policies and processes for managing capital.

### *Inventories*

The CICA issued Handbook Section 3031, *Inventories*, in March 2007, which is based on International Accounting Standard ("IAS") 2. The section replaced the existing Handbook Section 3030, *Inventories*. Under this section, inventories are required to be measured at the lower of cost and net realizable value, which is different from the existing guidance of lower of cost and market. This section also allows the reversal of any write-downs previously recognized. Further, due to the changes in the section and the consequential amendments, some of OPG's critical spare parts, which were previously reported as materials and supplies on OPG's consolidated balance sheets are now accounted for as property, plant and equipment. The accounting standard and the consequential amendments were effective for OPG beginning January 1, 2008. OPG reclassified significant critical spare parts of \$19 million, net of accumulated depreciation, to property, plant and equipment in 2008. This accounting standard and the consequential amendments did not have a significant impact to OPG's financial position or results of operations for the three and nine months ended September 30, 2008.

## *Intangible Assets*

In February 2008, the CICA issued Handbook Section 3064, *Goodwill and Intangible Assets*, which replaces Handbook Section 3062, *Goodwill and Other Intangible Assets*, and establishes standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. This section applies to annual and interim financial statements relating to fiscal years beginning on or after October 1, 2008, with early adoption encouraged. The adoption of this standard is not expected to have a significant impact on the Company's financial position or results of operations.

### **3. INVESTMENTS IN ASSET-BACKED COMMERCIAL PAPER**

In August 2007, the Asset Backed Commercial Paper ("ABCP") market experienced a liquidity event when paper sponsored by third-party non-bank conduits could not be refinanced as it matured. At that time, OPG's total ABCP investment was \$103 million. Of that amount, \$45 million was restructured, with OPG receiving payment of approximately 98.7 per cent of the face value of the notes in December 2007. Of the remaining \$58 million, OPG recorded an impairment loss of \$9 million as at December 31, 2007, plus an additional \$9 million impairment loss during the first quarter of 2008. The impairment loss was recorded in other losses. OPG's remaining holdings of third-party ABCP are recorded as long-term investments.

The remaining investment of \$58 million is subject to a restructuring proposal put forward by a committee of large noteholders (the "Plan"). The Plan provides that most of the assets in existing conduits be transferred into new conduits against which new long-term notes would be issued. The Plan was approved by the noteholders in April 2008 and sanctioned by the Ontario Superior Court in June 2008. On September 19, 2008, the Supreme Court of Canada ruled it would not hear a challenge to the restructuring by a group wanting to appeal the Plan. This cleared a major hurdle for the committee to start implementing the restructuring plan. OPG expects to receive new notes that will mature in approximately eight years, and will monitor the development of a secondary market to assess the fair value of its remaining holdings.

OPG has sufficient credit facilities to satisfy its financial obligations as they come due and does not expect any material adverse impact on its operations as a result of this current third-party ABCP liquidity issue.

### **4. SALE OF ACCOUNTS RECEIVABLE**

The Company has 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 accounts receivable reported and securitized by the Company are as follows:

<i>(millions of dollars)</i>	<b>Principal Amount of Receivables</b>	
	<b>September 30</b>	<b>December 31</b>
	<b>2008</b>	<b>2007</b>
Total receivables portfolio <sup>1</sup>	<b>439</b>	479
Receivables sold	<b>300</b>	300
Receivables retained	<b>139</b>	179

<sup>1</sup> Amount represents receivables outstanding, including receivables that have been securitized, which the Company continues to service.

The pre-tax charges and average cost of funds are as follows:

<i>(millions of dollars)</i>	<b>Three Months Ended September 30</b>		<b>Nine Months Ended September 30</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
Pre-tax charges	<b>3</b>	<b>4</b>	<b>9</b>	<b>11</b>
Average cost of funds <i>(per cent)</i>	<b>3.7</b>	<b>5.2</b>	<b>4.1</b>	<b>5.0</b>

## **5. FIXED ASSETS, DEPRECIATION AND AMORTIZATION**

Depreciation and amortization expense for the three and nine months ended September 30, 2008 and 2007 consists of the following:

<i>(millions of dollars)</i>	<b>Three Months Ended September 30</b>		<b>Nine Months Ended September 30</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
Depreciation	<b>157</b>	<b>144</b>	<b>456</b>	<b>435</b>
Amortization of deferred Pickering A return to service costs	<b>3</b>	<b>20</b>	<b>36</b>	<b>76</b>
Nuclear waste management costs	<b>2</b>	<b>4</b>	<b>5</b>	<b>8</b>
	<b>162</b>	<b>168</b>	<b>497</b>	<b>519</b>

Interest capitalized to construction in progress at six per cent during the three and nine months ended September 30, 2008 (three and nine months ended September 30, 2007 – six per cent) was \$15 million and \$41 million, respectively (three and nine months ended September 30, 2007 – \$11 million and \$29 million, respectively).

## **6. REGULATORY ASSETS AND LIABILITIES AND SUMMARY OF RATE REGULATED ACCOUNTING**

Under a regulation introduced pursuant to the *Electricity Restructuring Act, 2004* (Ontario), OPG was required to establish certain variance and deferral accounts. OPG ceased recording additions to these variance and deferral accounts (with the exception of interest) as of April 1, 2008 pending a decision from the OEB in relation to its rate application for new payment amounts. OPG continued to amortize the Pickering A return to service deferral account in the second and third quarters of 2008 as the balance in this account was being recovered through existing rates.

In accordance with the regulation pursuant to the *Electricity Restructuring Act, 2004* (Ontario), OPG has recorded interest on its regulatory assets and liabilities balances at the rate of six per cent for the period from April 1, 2005 to March 31, 2008. OPG continued to record interest on the outstanding balances at six per cent during the six months ended September 30, 2008, pending the OEB's decision on its application for new payment amounts.

The regulatory assets and liabilities recorded as at September 30, 2008 and December 31, 2007 are as follows:

<i>(millions of dollars)</i>	<b>September 30 2008</b>	<b>December 31 2007</b>
<b>Regulatory assets</b>		
Pickering A return to service costs	<b>154</b>	183
Nuclear liabilities deferral account	<b>168</b>	131
Nuclear generation development costs – Capacity refurbishment	<b>17</b>	16
Nuclear generation development costs – New nuclear development	<b>16</b>	12
Hydroelectric production variance	<b>8</b>	7
Ancillary services revenue variance	<b>5</b>	5
Transmission outages and transmission restrictions variance	<b>2</b>	2
<b>Total regulatory assets</b>	<b>370</b>	356
<b>Regulatory liabilities</b>		
Other	<b>13</b>	14
<b>Total regulatory liabilities</b>	<b>13</b>	14

The changes in the regulatory assets and liabilities for the nine months ended September 30, 2008 and the year ended December 31, 2007 are as follows:

<i>(millions of dollars)</i>	<b>Pickering A Return to Service Costs</b>	<b>Nuclear Liabilities Deferral Account</b>	<b>Nuclear Generation Development Costs – Capacity Refurbishment</b>	<b>Nuclear Generation Development Costs – New Nuclear Development</b>	<b>Transmission Outages and Transmission Restriction Variance</b>	<b>Hydro- electric Production Variance</b>	<b>Ancillary Services Revenue Variance</b>	<b>Other</b>
Regulatory assets (liabilities), January 1, 2007	249	-	-	-	2	(4)	-	(7)
Increase (decrease) during the year	-	128	15	12	-	11	5	(5)
Interest	30	3	1	-	-	-	-	(2)
Amortization during the year	(96)	-	-	-	-	-	-	-
Regulatory assets (liabilities), December 31, 2007	183	131	16	12	2	7	5	(14)
Increase during the period	-	31	-	4	-	1	-	1
Interest	7	6	1	-	-	-	-	-
Amortization during the period	(36)	-	-	-	-	-	-	-
Regulatory assets (liabilities), September 30, 2008	<b>154</b>	<b>168</b>	<b>17</b>	<b>16</b>	<b>2</b>	<b>8</b>	<b>5</b>	<b>(13)</b>

### **Nuclear Generation Development Costs**

Based on amendments to the regulation pursuant to the *Electricity Restructuring Act, 2004* (Ontario) made in February 2007 and February 2008, OPG recorded regulatory assets related to non-capital costs for nuclear generation development initiatives up to March 31, 2008. Specifically, the costs recorded were those made in the course of planning and preparing for the development of proposed new nuclear

facilities, as well as those related to the potential refurbishment at the Pickering B and Darlington nuclear stations to the extent that they had not been previously included in the forecast provided to the Province of Ontario (the "Province") for the purposes of establishing rates for the period from April 1, 2005 to March 31, 2008. OPG recorded costs totalling \$16 million related to the new nuclear generation development initiatives and \$16 million related to the potential refurbishment of existing stations as regulatory assets up to March 31, 2008.

### Summary of Rate Regulated Accounting

The following tables summarize the impact of applying rate regulated accounting for selected income statement information:

<i>(millions of dollars)</i>	Three Months Ended September 30 2008			Three Months Ended September 30 2007		
	As Stated	Impact of Rate Regulated Accounting	Financial Statements without Rate Regulated Accounting	As Stated	Impact of Rate Regulated Accounting	Financial Statements without Rate Regulated Accounting
	Revenue	1,513	5	1,518	1,421	10
Fuel expense	334	-	334	336	(1)	335
Operations, maintenance, and administration	689	-	689	689	6	695
Depreciation and amortization	162	(3)	159	168	(8)	160
Accretion on fixed asset removal and nuclear waste management liabilities	151	-	151	127	18	145
Property and capital taxes	24	-	24	17	1	18
Net interest expense	41	3	44	37	4	41

<i>(millions of dollars)</i>	Nine Months Ended September 30 2008			Nine Months Ended September 30 2007		
	As Stated	Impact of Rate Regulated Accounting	Financial Statements without Rate Regulated Accounting	As Stated	Impact of Rate Regulated Accounting	Financial Statements without Rate Regulated Accounting
	Revenue	4,461	14	4,475	4,318	22
Fuel expense	915	(2)	913	962	(4)	958
Operations, maintenance, and administration	2,130	4	2,134	2,159	20	2,179
Depreciation and amortization	497	(23)	474	519	(36)	483
Accretion on fixed asset removal and nuclear waste management liabilities	438	19	457	381	56	437
Property and capital taxes	54	1	55	66	3	69
Net interest expense	120	14	134	102	29	131

## 7. LONG-TERM DEBT

Long-term debt consists of the following:

<i>(millions of dollars)</i>	September 30 2008	December 31 2007
Notes payable to the Ontario Electricity Financial Corporation	3,640	3,665
Share of non-recourse limited partnership debt	182	188
	<b>3,822</b>	<b>3,853</b>
Less: due within one year		
Notes payable to the Ontario Electricity Financial Corporation	350	400
Share of limited partnership debt	7	7
	<b>357</b>	<b>407</b>
Long-term debt	<b>3,465</b>	<b>3,446</b>

Interest paid during the three months ended September 30, 2008 was \$104 million (three months ended September 30, 2007 – \$90 million), of which \$98 million relates to interest paid on long-term debt (three months ended September 30, 2007 – \$86 million). Interest paid during the nine months ended September 30, 2008 was \$218 million (nine months ended September 30, 2007 – \$200 million), of which \$205 million relates to interest paid on long-term debt (nine months ended September 30, 2007 – \$187 million). Interest on the notes payable to the Ontario Electricity Financial Corporation (“OEFC”) is paid semi-annually.

Debt financing for the Niagara Tunnel, the Portlands Energy Centre and the Lac Seul hydroelectric generating station projects is provided by the OEFC. As at September 30, 2008, debt financing for these projects consists of the following:

<i>(millions of dollars)</i>	Niagara Tunnel	Portlands Energy Centre	Lac Seul Hydroelectric Generating Station
Debt financing, as at December 31, 2007	240	210	20
New borrowing	100	75	-
Debt financing, as at September 30, 2008	<b>340</b>	<b>285</b>	<b>20</b>

## 8. SHORT-TERM CREDIT FACILITIES AND NET INTEREST EXPENSE

OPG maintains a \$1 billion revolving committed bank credit facility which is divided into two tranches – a \$500 million 364-day term tranche and a \$500 million five-year term tranche. OPG renewed and extended the maturity date of the 364-day term tranche to May 20, 2009 and the five-year term tranche to May 20, 2013. The total credit facility will continue to be used primarily as credit support for notes issued under OPG’s commercial paper program. As at December 31, 2007 and September 30, 2008, no commercial paper was outstanding, and OPG had no other outstanding borrowings under the bank credit facility. In the second quarter of 2008, OPG entered into a \$100 million five-year revolving committed bank credit facility in support of the Upper Mattagami Project. As at September 30, 2008, there was no borrowing under this credit facility.

The following table summarizes the net interest expense for the three and nine months ended September 30, 2008 and 2007:

<i>(millions of dollars)</i>	<b>Three Months Ended September 30</b>		<b>Nine Months Ended September 30</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
Interest on long-term debt	<b>60</b>	50	<b>174</b>	150
Interest on short-term debt	<b>4</b>	4	<b>11</b>	14
Interest income	<b>(4)</b>	(2)	<b>(10)</b>	(4)
Capitalized interest	<b>(15)</b>	(11)	<b>(41)</b>	(29)
Other	<b>(4)</b>	(4)	<b>(14)</b>	(29)
<b>Net interest expense</b>	<b>41</b>	37	<b>120</b>	102

#### **9. 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>	<b>September 30 2008</b>	<b>December 31 2007</b>
Liability for nuclear used fuel management	<b>6,144</b>	5,938
Liability for nuclear decommissioning and low and intermediate level waste management	<b>4,987</b>	4,843
Liability for non-nuclear fixed asset removal	<b>182</b>	176
<b>Fixed asset removal and nuclear waste management liabilities</b>	<b>11,313</b>	10,957

The change in the fixed asset removal and nuclear waste management liabilities for the nine months ended September 30, 2008 and the year ended December 31, 2007 are as follows:

<i>(millions of dollars)</i>	<b>September 30 2008</b>	<b>December 31 2007</b>
Liabilities, beginning of period	<b>10,957</b>	10,520
Increase in liabilities due to accretion	<b>457</b>	582
Increase in liabilities due to nuclear used fuel and nuclear waste management variable expenses	<b>34</b>	76
Liabilities settled by expenditures on waste management	<b>(135)</b>	(200)
Decrease in the liabilities for non-nuclear fixed asset removal	<b>-</b>	(21)
<b>Liabilities, end of period</b>	<b>11,313</b>	10,957

## Ontario Nuclear Funds Agreement

OPG sets aside and invests funds held in segregated custodian and trustee 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 September 30, 2008 and December 31, 2007 consist of the following:

<i>(millions of dollars)</i>	Fair Value	
	September 30 2008	December 31 2007
Decommissioning Fund	4,624	5,075
Due to Province – Decommissioning Fund	-	(3)
	<b>4,624</b>	<b>5,072</b>
Used Fuel Fund <sup>1</sup>	4,596	4,702
Due from (to) Province – Used Fuel Fund	196	(511)
	<b>4,792</b>	<b>4,191</b>
	<b>9,416</b>	<b>9,263</b>

<sup>1</sup> The Ontario NFWA Trust represented \$1,357 million as at September 30, 2008 (December 31, 2007 - \$1,244 million) of the Used Fuel Fund on a fair value basis.

## 10. INCOME TAXES

The following table summarizes the difference in the interim consolidated statements of (loss) income under the taxes payable method used by the Company to account for income taxes for the regulated business compared to what would have been reported had OPG applied the liability method for the regulated business for the three and nine months ended September 30, 2008 and 2007:

<i>(millions of dollars)</i>	Three Months Ended September 30		Nine Months Ended September 30	
	2008	2007	2008	2007
As stated:				
Future income tax expense (recovery)	31	5	(131)	14
Future income tax: Other comprehensive income – Upon transition	-	-	-	16
Future income tax: Other comprehensive income – for the period	3	(2)	(3)	(3)
Liability method:				
Future income tax expense (recovery)	(47)	24	(94)	75
Future income tax: Other comprehensive income – Upon transition	-	-	-	12
Future income tax: Other comprehensive income – for the period	4	(7)	(7)	1

The following table summarizes the difference in the interim consolidated balance sheets under the taxes payable 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 as at September 30, 2008 and December 31, 2007:

<i>(millions of dollars)</i>	<b>September 30, 2008</b>		<b>December 31, 2007</b>	
	<b>As Stated<sup>1</sup></b>	<b>Liability Method<sup>1,2</sup></b>	<b>As Stated<sup>1</sup></b>	<b>Liability Method<sup>1,2</sup></b>
Future income tax assets – current	<b>5</b>	<b>32</b>	12	39
Long-term future income tax assets	<b>24</b>	-	-	-
Long-term future income tax liabilities	-	<b>(472)</b>	(217)	(680)

<sup>1</sup>The amounts include the impact of the resolution of a number of tax uncertainties.

<sup>2</sup> The amounts of future income taxes not recorded do not include the future income taxes resulting from regulatory assets and liabilities that would be recorded effective January 1, 2008 due to amendments to CICA Handbook Section 3465, *Income Taxes*.

In the third quarter of 2006, OPG received a preliminary communication from the Provincial Tax Auditors (“Tax Auditors”) with respect to their initial findings from their audit of OPG’s 1999 taxation year. Many of the issues raised through the audit were unique to OPG and relate either to start-up matters and positions taken on April 1, 1999 upon commencement of operations, or matters that were not adequately addressed through the *Electricity Act, 1998*. In 2008, all outstanding tax matters related to the 1999 tax audit were resolved. As a result, OPG reduced its income tax liability by \$106 million.

On November 3, 2008, the OEB issued its decision on OPG’s application for new payment amounts, which included the approval of a taxation variance account for the period retrospectively beginning on April 1, 2008. The scope of the account with respect to income taxes includes variances in the income tax expense for the Company’s rate regulated segments caused by changes in tax rates or rules under the *Income Tax Act (Canada)* and the *Corporations Tax Act (Ontario)*, as modified by the *Electricity Act, 1998*, as well as variances caused by reassessments due to audits of OPG’s taxation years subsequent to 1999. Variances are determined with respect to the forecast approved by the OEB in the setting of OPG’s payment amounts for production from its rate regulated operations. OPG does not expect to record any amounts in the account for the period April 1, 2008 to September 30, 2008 during the fourth quarter of 2008.

The amount of cash income taxes paid during the three months ended September 30, 2008 was \$14 million (three months ended September 30, 2007 – nil). For the nine months ended September 30, 2008, cash income taxes paid were \$44 million (nine months ended September 30, 2007 - \$52 million).

## 11. PENSION AND OTHER POST EMPLOYMENT BENEFIT COSTS

Total benefit costs for the three and nine months ended September 30, 2008 and 2007, are as follows:

<i>(millions of dollars)</i>	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30 2008</b>	<b>September 30 2007</b>	<b>September 30 2008</b>	<b>September 30 2007</b>
Registered pension plan	<b>47</b>	61	<b>141</b>	182
Supplementary pension plans	<b>4</b>	4	<b>12</b>	11
Other post employment benefits	<b>52</b>	60	<b>162</b>	175

## 12. FINANCIAL INSTRUMENTS

OPG's Board of Directors has approved, and management has implemented, a risk management governance structure designed to effectively identify, measure, monitor and report on key risks across the Company. Risk management activities are coordinated through a centralized risk management group, separate and independent from operational management. Risk information from the business units is independently assessed and aggregated by the Risk Services Group, and is reported by the Chief Risk Officer to the Executive Risk Committee and to the Audit/Risk committee of the Board. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Company's activities.

OPG is exposed to risks related to changes in electricity prices associated with a wholesale spot market for electricity in Ontario, changes in interest rates, and movements in foreign currency that affect its assets, liabilities, and forecast transactions. Select derivative instruments are used to limit such risks. Derivatives are used as hedging instruments, as well as for trading purposes.

The following is a summary of OPG's financial instruments as at September 30, 2008:

<b>Financial Instruments <sup>1</sup></b> <i>(millions of dollars)</i>	<b>Designated Category</b>	<b>Fair Value</b>
Cash and cash equivalents	Held-to-maturity	<b>483</b>
Long-term investments <sup>2</sup>	Held-to-maturity	<b>40</b>
Nuclear fixed asset removal and nuclear waste management funds	Held-for-trading	<b>9,416</b>
Long-term debt (including current portion)	Other liabilities	<b>3,827</b>
Other commodity derivative instruments included in current and long-term accounts receivable <sup>3</sup>	Held-for-trading	<b>23</b>
Other commodity derivative instruments included in current and long-term accounts payable <sup>3</sup>	Held-for-trading	<b>(18)</b>

<sup>1</sup> The carrying value of other financial instruments included in accounts receivable and accounts payable and accrued charges approximates their fair value due to the immediate or short-term maturity of these financial instruments.

<sup>2</sup> Excludes investments of \$42 million owned by the Company's wholly-owned subsidiary, OPG Ventures Inc., that are recorded at fair value in accordance with Accounting Guideline 18, *Investment Companies*.

<sup>3</sup> Derivative instruments not qualifying for hedge accounting.

### Risks Associated with Financial Instruments

#### *Credit Risk*

Credit risk is the risk that counterparty to a financial instrument might fail to meet its obligation under the terms of a financial instrument. To manage credit risk, the Company enters into transactions with creditworthy counterparties, limits the amount of exposure to each counterparty where possible, and monitors the financial condition of counterparties.

The following table provides information on credit risk from energy trading activities as at September 30, 2008:

Credit Rating <sup>1</sup>	Number of Counterparties <sup>2</sup>	Potential Exposure for Largest Counterparties		
		Potential Exposure <sup>3</sup> <i>(millions of dollars)</i>	Number of Counterparties	Counterparty Exposure <i>(millions of dollars)</i>
Investment grade	26	94	4	61

<sup>1</sup> Credit ratings are based on OPG's own analysis, taking into consideration external rating agency analysis where available, as well as recognizing explicit credit support provided through guarantees and letters of credit or other security.

<sup>2</sup> OPG's counterparties are defined by each master agreement.

<sup>3</sup> Potential exposure is OPG's assessment of maximum exposure over the life of each transaction at a 95 per cent confidence interval.

The majority of OPG's revenues are derived from sales through the IESO administered spot market. Net credit exposure to the IESO at September 30, 2008 was \$139 million (Note 4). Although the credit exposure to the IESO represents a significant portion of OPG's accounts receivable, the Company's management accepts this risk due to the IESO's primary role in the Ontario electricity market. The remaining receivables exposure was a diverse group of generally high quality counterparties. OPG's allowance for doubtful debts at September 30, 2008 was less than \$1 million.

OPG also enters into financial transactions with highly rated financial institutions in order to hedge interest rate and currency exposures. The potential credit exposure with these counterparties was less than \$15 million at September 30, 2008. Other credit exposures include the investing of excess cash.

#### Investments

The Company limits its exposure to credit risk by investing in reasonably liquid (i.e. in normal circumstances, capable of liquidation within one month) securities that are rated by a recognized credit rating agency in accordance with a minimum investment quality standards. In regard to derivative contracts, the Company limits its exposure to credit risk by engaging with high credit-quality counterparties.

Current exposure to credit risk has changed due to the Company's exposure to the restructuring of the ABCP market in Canada. Additional details with respect to OPG's exposure to the restructuring program are described in Note 3.

#### Guarantees

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

#### *Liquidity Risk*

Liquidity risk arises through excess financial obligations over available financial assets, due at any point in time. The Company's approach to managing liquidity is to continuously monitor its ability to maintain sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses.

The table below summarizes the maturity profile of the Company's long-term debt at September 30, 2008:

<i>(millions of dollars)</i>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013 and Thereafter</b>
Long-term debt	357	978	383	409	1,694
Interest on long-term debt	214	182	133	105	457

Non-recourse limited partnership debt is secured by a first charge on the assets of one of the joint venture limited partnerships, an assignment of the joint venture's bank accounts, and an assignment of the joint venture's project agreements.

#### *Market Risk*

Market risk is the risk that changes to market prices, such as foreign exchange rates, interest rates, electricity prices and equities, will affect OPG's income or the value of the Company's holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return on risk.

The Company manages its exposure to market risks using forwards and various derivative products in the ordinary course of business. All such transactions are carried out within the guidelines set by the Executive Risk Committee.

#### Foreign Exchange Risk

OPG's foreign exchange exposure is attributable to two primary factors: United States dollar ("USD") denominated transactions such as the purchase of fossil fuels; and the influence of USD denominated commodity prices on Ontario electricity spot market prices. OPG enters into derivative contracts with major financial institutions to manage the Company's exposure to foreign currency movements.

#### Interest Rate Risk

Interest rate risk is the risk that the value of OPG's assets and liabilities can decrease and increase respectively because of a change in the related interest rates. OPG considers interest rate risk related to cash and cash equivalents and short-term borrowings to be low because of their short-term nature. Changes in interest rates do not currently have a significant impact on the Company's interest expense, since long-term borrowings are on a fixed rate basis.

The Company is exposed to interest rate risk on its long-term borrowings expected to be issued in the future. The Company manages the exposure to changes in market interest rates on anticipated issuance of long-term borrowings by entering into forward start interest rate contracts and floating-to-fixed interest rate swap contracts.

#### Electricity Price Risk

Electricity price risk for the Company is the potential for adverse movements in the market price of electricity. Exposure to electricity price risk is reduced as a result of regulated rates for a significant portion of OPG's business, and is also affected by the revenue limit rebate mechanism that applies to generation from OPG's unregulated generating stations. To manage this risk, the Company seeks to maintain a balance between the commodity price risk inherent in its electricity production and electricity forward sales contracts to the extent that trading liquidity in the electricity commodity market provides the economic opportunity to do so.

The table below summarizes a sensitivity analysis for significant unsettled market risk exposures with respect to the Company's financial instruments as at September 30, 2008, with all other variables held

constant. It shows how net income and other comprehensive income before tax would have been affected by changes in the relevant risk variable that were reasonably possible, at that date, over a three-month period.

<i>(millions of dollars except where noted)</i>	<b>A Change of:</b>	<b>Impact on Net Income Before Tax</b>	<b>Impact on Other Comprehensive Income Before Tax</b>
Foreign exchange – U.S. dollar	+/- 0.02	-	1
Interest rate <sup>1</sup>	+/- 10 basis points	-	+3/-4
Electricity price – Hedge <sup>2</sup>		n/a	3
Electricity price – Trading <sup>2</sup>		2	n/a

<sup>1</sup> The interest rate sensitivity analysis was determined based on the exposure to interest rates for derivatives instruments designated as hedges at the dates of the interim consolidated balance sheets.

<sup>2</sup> The sensitivity analysis around electricity prices was constructed using forward price volatilities that were based on historical daily forward electricity contract prices. The analysis considered contracts of varying time frames, traded in Ontario and neighbouring electricity markets.

### *Nuclear Funds Equity Price Risk*

Equity price risk is the risk of loss or unexpected volatility due to a decline in the values of individual equities and/or equity indices. The Company is exposed to equity price risk primarily related to equity investments held in the Nuclear Funds that are classified on the interim consolidated balance sheets as held-for-trading and measured at fair value. To manage this risk, OPG has established investment policies and procedures that set out an investment framework for the funds, including the investment assumptions, permitted investments, and various investment constraints for the Nuclear Funds. Such policies and procedures are approved annually by OPG and the Province in the case of the Decommissioning Fund and by the Province in the case of the Used Fuel Fund.

Under the Ontario Nuclear Funds Agreement, the annual return in the Used Fuel Fund is guaranteed by the Province for funding related to the first 2.23 million used fuel bundles. Therefore, OPG is not currently exposed to equity price risk in the Used Fuel Fund. OPG is, however, exposed to equity price risk in the Decommissioning Fund. Due to the long-term nature of the Decommissioning Fund's liabilities, the target asset mix of the fund was established with the goal of meeting the long-term liabilities. As such, the Company is prepared to accept shorter term market fluctuations with the expectation that equity securities will provide adequate returns over the long term.

The table below approximates the potential dollar impact on OPG's pre-tax profit, associated with a 1 per cent change in the specified equity indices. This analysis is based on the market values of the Decommissioning Fund's equity holdings at September 30, 2008, as well as on the assumption that when one equity index changes by 1 per cent, all other equity indices are held constant.

<i>(millions of dollars)</i>	<b>September 30 2008</b>
S&P/TSX Capped Composite Index	<b>12</b>
S&P 500	<b>4</b>
MSCI EAFE Index	<b>4</b>
MSCI World Index	<b>5</b>

### **Derivatives and Hedging**

At the inception of a hedging relationship, OPG documents the relationship between the hedging instrument and the hedged item, its risk management objective and its strategy for undertaking the

hedge. OPG also requires a documented assessment, both at hedge inception and on an ongoing basis, of whether or not the derivatives that are used in hedging transactions are highly effective in offsetting the changes attributable to the hedged risks in the fair values or cash flows of the hedged items.

Hedge accounting is applied when the derivative instrument is designated as a hedge and is expected to be effective throughout the life of the hedged item. When such a derivative instrument hedge ceases to exist or be effective as a hedge, or when designation of a hedging relationship is terminated, any associated deferred gains or losses are carried forward to be recognized in income in the same period as the corresponding gains or losses associated with the hedged item. When a hedged item ceases to exist, any associated deferred gains or losses are recognized in the current period's consolidated statement of (loss) income.

*Derivative Instruments Qualifying for Hedge Accounting*

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 in net (loss) income 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>	<b>Notional Quantity September 30, 2008</b>	<b>Terms</b>	<b>Fair Value</b>	<b>Notional Quantity December 31, 2007</b>	<b>Terms</b>	<b>Fair Value</b>
Electricity derivative instruments	<b>1.1 TWh</b>	<b>1-2 yrs</b>	<b>24</b>	1.8 TWh	1-3 yrs	35
Foreign exchange derivative instruments	<b>U.S. \$50</b>	<b>May/09</b>	<b>2</b>	U.S. \$48	Sep./08	(1)
Floating to fixed interest rate hedges	<b>41</b>	<b>1-11 yrs</b>	<b>(3)</b>	43	1-11 yrs	(2)
Forward start interest rate hedges	<b>322</b>	<b>1-12 yrs</b>	<b>(17)</b>	692	1-12 yrs	(6)

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 September 30, 2008 and December 31, 2007 was U.S. \$0.99 for every Canadian dollar.

One of the Company's joint ventures is exposed to changes in interest rates. The joint venture entered into an interest rate swap to manage the risk arising from fluctuations in interest rates by swapping the short-term floating interest rate with a fixed rate of 5.33 per cent. OPG's proportionate interest in the swap is 50 per cent and is accounted for as a hedge.

Net losses of \$3 million and \$7 million related to derivative instruments qualifying for hedge accounting were recognized in net (loss) income during the three and nine months ended September 30, 2008, respectively. This amount was previously recorded in other comprehensive (loss) income. Existing net gains of \$12 million deferred in accumulated other comprehensive (loss) income at September 30, 2008 are expected to be reclassified to net (loss) income within the next 12 months.

In the third quarter of 2008, OPG de-designated certain forward start interest rate hedges as the previously anticipated future borrowings associated with these instruments were no longer expected to occur. As a result of the de-designation, a net loss of \$3 million was reclassified to net (loss) income in the third quarter of 2008.

### *Derivative Instruments Not Qualifying for Hedge Accounting*

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

<i>(millions of dollars except where noted)</i>	<b>Notional Quantity September 30, 2008</b>	<b>Fair Value</b>	<b>Notional Quantity December 31, 2007</b>	<b>Fair Value</b>
Foreign exchange derivative instruments	-	-	U.S.\$14	(2)
Commodity derivative instruments				
Assets	<b>4.4 TWh</b>	<b>23</b>	9.9 TWh	14
Liabilities	<b>2.3 TWh</b>	<b>(18)</b>	1.2 TWh	(10)
Market liquidity reserve		<b>5</b>		2
		<b>(12)</b>		(2)
<b>Total</b>		<b>(7)</b>		-

Foreign exchange derivative instruments that are not designated as hedges have a weighted average exchange rate of U.S. \$0.86 at December 31, 2007.

### **Fair Value**

Fair value is the value that a financial instrument can be closed out or sold, in a transaction with a willing and knowledgeable counterparty. The fair value of financial assets and liabilities, including exchange traded derivatives and other financial instruments for which quoted prices are available in an active market, are determined directly from those quoted market prices.

For financial instruments which do not have quoted market prices directly available, fair values are estimated using forward price curves developed from observable market prices or rates which may include the use of valuation techniques or models, based, wherever possible, on assumptions supported by observable market prices or rates prevailing at the dates of the interim consolidated balance sheets. This is the case for over-the-counter derivatives and securities, which include energy commodity derivatives, foreign exchange derivatives, interest rate swap derivatives, and ABCP issued by third-party trusts. Valuation models use general assumptions and market data and therefore do not reflect the specific risks and other factors that would affect a particular instrument's fair value. The methodologies used for calculating the fair value adjustments are reviewed on an ongoing basis to ensure that they remain appropriate.

Forward pricing information is inherently uncertain so that fair values of derivative instruments may not accurately represent the cost to enter into these positions. To address the impact of some of this uncertainty on trading positions, OPG established liquidity reserves against the mark-to-market gains or losses of these positions. These reserves increased trading revenue by \$7 million during the three months ended September 30, 2008 (three months ended September 30, 2007 – decreased by \$1 million). During the nine months ended September 30, 2008, the reserves decreased trading revenue by \$10 million (nine months ended September 30, 2007 – decreased by \$1 million).

### **13. CAPITAL MANAGEMENT**

The Board of Director's objectives when managing capital are to safeguard the Company's assets and its ability to operate on a commercial basis, while undertaking future development projects that provide an adequate return to the shareholder, and benefits to other stakeholders. The Company attempts to maintain an optimal capital structure and minimize the cost of capital.

The Company is owned 100 per cent by the Province. To minimize its cost of capital, the Company targets financial metrics consistent with an investment grade credit rating. This provides the Company with access to capital markets in the future, while targeting a low cost of debt financing.

The Company monitors capital on the basis of the ratio of total debt to total capitalization. Debt is calculated as total borrowings, including long-term debt due within one year, long-term debt and the amount of the letters of credit. Total capitalization is calculated as total debt plus total shareholder's equity as shown in the interim consolidated balance sheets. A financial covenant in OPG's \$1 billion revolving committed bank credit facility requires OPG to maintain on a fully consolidated basis, a ratio of debt to total capitalization of not greater than 0.65:1.0 at any time.

As per the November 3, 2008 OEB decision, the deemed capital structure for the regulated business is 53 per cent debt and 47 per cent equity.

The table below summarizes OPG's debt to total capitalization position:

<i>(millions of dollars)</i>	<b>September 30 2008</b>	<b>December 31 2007</b>
Long-term debt due within one year	<b>357</b>	407
Long-term debt	<b>3,465</b>	3,446
Letters of Credit	<b>243</b>	205
Total debt	<b>4,065</b>	4,058
Total shareholder's equity	<b>6,899</b>	6,807
Total capitalization	<b>10,964</b>	10,865
Total debt to total capitalization	<b>37%</b>	37%

There were no changes in the Company's approach to capital management during the period.

#### **14. 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.

On August 9, 2006, a Notice of Action and Statement of Claim in the amount of \$500 million (the "Claim") was served on OPG and Bruce Power L.P. by British Energy Limited and British Energy International Holdings Limited ("British Energy"), claiming that OPG is liable to them for breach of contract and negligence. OPG leased the Bruce nuclear generating stations to Bruce Power L.P. in 2001. British Energy was an investor in Bruce Power L.P. In 2003, British Energy sold its interest in Bruce Power L.P. to a group of investors (the "Purchasers"). The Purchasers are claiming that British Energy is liable to them with respect to this purchase transaction. Their claim is currently the subject of an arbitration proceeding (the "Arbitration"). British Energy is therefore suing OPG in order to preserve any similar claim it may have against OPG pursuant to the 2001 lease transaction. British Energy has indicated that it does not require OPG to actively defend the Claim at this point in time as British Energy is defending the Arbitration commenced by the Purchasers. The Arbitration is scheduled to proceed in September 2009. It may narrow or eliminate the claims or damages British Energy has, so as to narrow or eliminate the need to continue the Claim against OPG. British Energy has reserved the right to require OPG to defend the Claim prior to the conclusion of the Arbitration should British Energy at some point believe there is some advantage in doing so.

On September 2, 2008, a certain First Nation has served a Notice of Action against Canada, Ontario, OPG and the OEFC claiming damages in the amount of \$200 million arising from breach of contract,

fiduciary duty, trespass to property, negligence, nuisance, misrepresentation, breach of riparian rights and unlawful and unjustifiable infringement of the aboriginal and treaty rights and \$0.5 million in special damages. A Notice of Arbitration was served the same time upon OPG pursuant to an agreement between OPG and the said First Nations to address OPG's role in the sharing of benefits related to hydro development. While OPG assesses the merits of the litigation, neither the arbitration nor the claim is likely to have any material impact on the Company's financial position, and therefore, OPG has minimal exposure with respect to this claim.

Certain First Nations have commenced actions for interference with reserve and traditional land rights. The claims by some of these First Nations total approximately \$40 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. As at September 30, 2008, the remaining provision was \$42 million (December 31, 2007 – \$45 million).

Current operations are subject to regulation with respect to emissions to air, water and land as well as 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 interim consolidated financial statements to meet OPG's current environmental obligations.

### **15. REVENUE LIMIT REBATE**

Eighty-five per cent of the generation output from OPG's unregulated generation assets, excluding the Lennox generating station and forward sales as of January 1, 2005, is subject to a revenue limit.

The change in the revenue limit rebate liability for the nine months ended September 30, 2008 and the year ended December 31, 2007 are as follows:

<i>(millions of dollars)</i>	<b>September 30 2008</b>	<b>December 31 2007</b>
Liability, beginning of period	<b>100</b>	40
Increase to provision during the period	<b>237</b>	227
Payments made during the period	<b>(189)</b>	(167)
Liability, end of period	<b>148</b>	100

## 16. BUSINESS SEGMENTS

Segment (Loss) Income for the Three Months Ended September 30, 2008	Regulated		Unregulated			Total
	Nuclear	Hydro- electric	Hydro- electric	Fossil- Fuelled	Other	
<i>(millions of dollars)</i>						
Revenue	697	187	250	437	57	1,628
Revenue limit rebate	-	-	(30)	(85)	-	(115)
	697	187	220	352	57	1,513
Fuel expense	43	69	31	191	-	334
Gross margin	654	118	189	161	57	1,179
Operations, maintenance and administration	478	21	48	129	13	689
Inter-segment service fee	7	1	1	2	(11)	-
Depreciation and amortization	94	16	19	22	11	162
Accretion on fixed asset removal and nuclear waste management liabilities	149	-	-	2	-	151
Losses on nuclear fixed asset removal and nuclear waste management funds	190	-	-	-	-	190
Property and capital taxes	11	2	3	5	3	24
(Loss) income before interest and income taxes	(275)	78	118	1	41	(37)

Segment Income (Loss) for the Three Months Ended September 30, 2007	Regulated		Unregulated			Total
	Nuclear	Hydro- electric	Hydro- electric	Fossil- Fuelled	Other	
<i>(millions of dollars)</i>						
Revenue	629	171	162	483	36	1,481
Revenue limit rebate	-	-	(16)	(44)	-	(60)
	629	171	146	439	36	1,421
Fuel expense	33	60	19	224	-	336
Gross margin	596	111	127	215	36	1,085
Operations, maintenance and administration	476	22	43	126	22	689
Inter-segment service fee	11	1	1	4	(17)	-
Depreciation and amortization	104	16	15	20	13	168
Accretion on fixed asset removal and nuclear waste management liabilities	124	-	-	3	-	127
Earnings on nuclear fixed asset removal and nuclear waste management funds	(92)	-	-	-	-	(92)
Property and capital taxes	3	3	3	5	3	17
(Loss) income before interest and income taxes	(30)	69	65	57	15	176

<b>Segment (Loss) Income for the Nine Months Ended September 30, 2008</b>	<b>Regulated</b>		<b>Unregulated</b>		<b>Other</b>	<b>Total</b>
	<b>Nuclear</b>	<b>Hydro- electric</b>	<b>Hydro- electric</b>	<b>Fossil- Fuelled</b>		
<i>(millions of dollars)</i>						
Revenue	2,055	556	776	1,217	94	4,698
Revenue limit rebate	-	-	(57)	(180)	-	(237)
	2,055	556	719	1,037	94	4,461
Fuel expense	120	185	84	526	-	915
Gross margin	1,935	371	635	511	94	3,546
Operations, maintenance and administration	1,506	68	138	381	37	2,130
Inter-segment service fee	21	2	3	6	(32)	-
Depreciation and amortization	295	48	55	68	31	497
Accretion on fixed asset removal and nuclear waste management liabilities	432	-	-	6	-	438
Losses on nuclear fixed asset removal and nuclear waste management funds	133	-	-	-	-	133
Property and capital taxes	14	8	7	16	9	54
(Loss) income before other gains and losses	(466)	245	432	34	49	294
Other (gains) and losses	-	-	-	(2)	9	7
(Loss) income before interest and income taxes	(466)	245	432	36	40	287

  

<b>Segment Income for the Nine Months Ended September 30, 2007</b>	<b>Regulated</b>		<b>Unregulated</b>		<b>Other</b>	<b>Total</b>
	<b>Nuclear</b>	<b>Hydro- electric</b>	<b>Hydro- electric</b>	<b>Fossil- Fuelled</b>		
<i>(millions of dollars)</i>						
Revenue	1,943	526	581	1,341	103	4,494
Revenue limit rebate	-	-	(48)	(128)	-	(176)
	1,943	526	533	1,213	103	4,318
Fuel expense	98	179	58	627	-	962
Gross margin	1,845	347	475	586	103	3,356
Operations, maintenance and administration	1,471	95	143	406	44	2,159
Inter-segment service fee	25	2	3	8	(38)	-
Depreciation and amortization	320	50	50	59	40	519
Accretion on fixed asset removal and nuclear waste management liabilities	374	-	-	7	-	381
Earnings on nuclear fixed asset removal and nuclear waste management funds	(392)	-	-	-	-	(392)
Property and capital taxes	23	10	8	16	9	66
Income before interest and income taxes	24	190	271	90	48	623

<i>(millions of dollars)</i>	Regulated		Unregulated			Total
	Nuclear	Hydro-electric	Hydro-electric	Fossil-Fuelled	Other	
<b>Selected Balance Sheet Information</b>						
As at September 30, 2008						
Segment fixed assets in service, net	3,858	3,838	2,970	393	484	11,543
Segment construction in progress	245	375	157	53	371	1,201
Segment property, plant and equipment, net	4,103	4,213	3,127	446	855	12,744
As at December 31, 2007						
Segment fixed assets in service, net	4,030	3,871	2,996	422	508	11,827
Segment construction in progress	210	299	88	49	304	950
Segment property, plant and equipment, net	4,240	4,170	3,084	471	812	12,777

#### 17. CHANGES IN NON-CASH WORKING CAPITAL BALANCES

<i>(millions of dollars)</i>	Three Months Ended September 30		Nine Months Ended September 30	
	2008	2007	2008	2007
Accounts receivable	145	66	105	(4)
Prepaid expenses	(14)	(33)	(4)	(33)
Fuel inventory	11	50	24	161
Materials and supplies	-	(3)	(3)	(7)
Revenue limit rebate	115	60	237	176
Accounts payable and accrued charges	(17)	(35)	(169)	(173)
Income and capital taxes payable	18	31	(7)	50
	258	136	183	170

#### 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 most of OPG's baseload hydroelectric facilities and all of the nuclear facilities that OPG operates, 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.

## 19. SUBSEQUENT EVENTS

### Impact of OEB Decision on Regulatory Assets and Liabilities

The OEB's decision on OPG's application for new payment amounts for its regulated hydroelectric and nuclear facilities was issued on November 3, 2008. The new payment amounts will include recovery of the retrospective increase in the payment amounts to April 1, 2008 and will be collected in the form of a rate rider on production from December 1, 2008 to December 31, 2009. The retrospective amount will be equal to the difference between the new payment amounts approved by the OEB and the existing payment amounts, multiplied by OPG's monthly forecast production for the period April 1, 2008 to November 30, 2008, included in the original application to the OEB.

In its decision on OPG's application, the OEB determined that the appropriate rate of return on equity for OPG's regulated facilities for the purposes of determining the new payment amounts is 8.65 per cent.

The OEB determined that the appropriate deemed capital structure, for the purposes of determining the new payment amounts, is 47 per cent equity and 53 per cent debt.

In its decision, the OEB approved the continuation of certain pre-existing variance and deferral accounts, established new variance accounts, and determined the disposition of balances in variance and deferral accounts as at December 31, 2007. OPG will apply for the disposition of regulatory balances recorded for the period from January 1, 2008 to March 31, 2008 in its next application to the OEB. OPG will begin amortizing the regulatory balances approved by the OEB in the fourth quarter of 2008.

The OEB approved all of OPG's regulatory assets and liabilities balances as at December 31, 2007 for recovery, with the exception of a portion of the regulatory asset related to nuclear generation development costs and the Other regulatory liability balance related to the segregated mode of operations and water transaction net revenue. As a result of these findings, OPG will write off a \$16 million regulatory asset balance and reverse a \$13 million regulatory liability in the fourth quarter of 2008.

The OEB approved the continuation of variance accounts associated with the impact of water conditions on hydroelectric production, ancillary services revenue retrospectively to April 1, 2008. The OEB also established variance accounts for nuclear fuel costs, new nuclear generation development costs, capacity refurbishment costs, revenues and costs associated with the stations on lease to Bruce Power LP ("Bruce Power"), and income and other taxes retrospective to April 1, 2008. The taxation costs variance account is described in Note 10.

The OEB established the recovery period for the Pickering A return to service deferral account as the 45-month period ending December 31, 2011. The OEB also approved the period of recovery for the nuclear deferral and variance accounts as the 33 months ending December 31, 2010. The hydroelectric variance accounts shall be recovered over the 21-month period ending December 31, 2009.

The variance account for revenues and costs associated with the nuclear generating stations on lease to Bruce Power was established by the OEB in conjunction with its determination that OPG's revenues and costs associated with ownership of these stations should be included in the determination of payment amounts for the prescribed nuclear facilities. A significant component of the regulatory asset relates to the losses on the Nuclear Funds related to the Bruce nuclear generating stations. Revenues associated with the leased nuclear generating stations reduce the payment amounts and costs associated with the stations are recovered through the payment amounts.

OPG is in the process of assessing the full impact of the OEB decision on its 2008 earnings, regulatory assets and regulatory liabilities. Once determined, this impact will be recorded in the fourth quarter of 2008.