

August 22, 2008

**ONTARIO POWER GENERATION REPORTS 2008 SECOND QUARTER FINANCIAL RESULTS**

[Toronto]: Ontario Power Generation Inc. (“OPG” or the “Company”) today reported its financial and operating results for the three and six months ended June 30, 2008. Net income for the second quarter of 2008 was \$99 million compared to net income of \$125 million for the same period in 2007. Net income for the six months ended June 30, 2008 was \$261 million compared to \$296 million for the same period in 2007.

“While OPG’s second quarter operational performance was essentially level with the second quarter of 2007, earnings on nuclear fixed asset removal and waste management segregated funds were lower as a result of the continued decline in the capital markets,” said President and CEO Jim Hankinson.

On June 16, 2008, the Province of Ontario (the “Province”) announced the selection of OPG as the operator of two new nuclear units that will be located at the Darlington site. “OPG takes great pride in being selected to operate these units at the Darlington site,” Hankinson said.

Electricity generated in the second quarter of 2008 was 25.9 terawatt hours (“TWh”) compared to production of 26.0 TWh in the second quarter of 2007. Hydroelectric production of 10.3 TWh was higher than production of 8.6 TWh during the second quarter of 2007 mainly due to higher river flows across the province. Nuclear production decreased by 1.0 TWh primarily as a result of outages at the Pickering B station. Electricity production from OPG’s fossil stations decreased to 5.5 TWh in the second quarter of 2008 compared to 6.3 TWh in 2007, primarily as a result of higher hydroelectric production. For the six months ended June 30, 2008, total production from OPG’s generating stations was 55.3 TWh compared to 54.2 TWh for the same period in 2007. This increase reflects higher hydroelectric and nuclear production partly offset by lower fossil production.

The reliability of OPG’s fossil and hydroelectric stations improved during the second quarter in comparison to the second quarter of 2007. Availability factors at OPG’s fossil stations have improved considerably over the past four years while availability factors at the Company’s hydroelectric stations remain near historically high levels. During the quarter, the Darlington nuclear station performed additional outage work resulting in a marginally lower capability factor compared to the second quarter of 2007. However, on a year to date basis, the station’s capability factor has improved. On a quarterly and year to date basis, capability factors at the Pickering A nuclear station continue to improve over 2007. While the availability of the Pickering B nuclear station has improved on a year to date basis over 2007, unplanned outages during the second quarter of 2007 had an unfavourable impact on the station’s capability factor.

Net income of \$99 million during the three months ended June 30, 2008 was lower than net income of \$125 million in the second quarter of 2007. Gross margin increased primarily due to higher generation from OPG's unregulated hydroelectric generating stations and a marginally higher electricity sales price, partially offset by lower generation from the nuclear and fossil-fuelled generating stations. Operations, Maintenance and Administration (OM&A) expenditures decreased primarily as a result of additional expenses related to past grievance settlements with First Nations that were incurred during the second quarter of 2007 and did not reoccur in 2008. Lower pension and other post employment benefits costs also contributed to this decrease in OM&A. Income tax expense decreased due to a reduction in income tax liabilities as a result of the resolution of a number of tax uncertainties. These favourable impacts were offset by a decrease in earnings on the nuclear fixed asset removal and nuclear waste management funds, primarily as a result of continuing significant volatility and unfavourable returns in the capital markets.

Net income of \$261 million during the six months ended June 30, 2008 was lower than net income of \$296 million for the same period in 2007. Gross margin increased primarily due to higher generation from OPG's unregulated hydroelectric stations and nuclear stations, partially offset by lower fossil generation. On a year to date basis, OM&A expenses, income taxes, and earnings on the nuclear fixed asset removal and nuclear waste management funds decreased for the same reasons as during the second quarter of 2008.

In May 2008, the Province announced limits on CO<sub>2</sub> emissions from OPG's coal-fired generating stations to ensure that such emissions are reduced by two-thirds below 2003 levels by 2011. The government has directed OPG to stage the reduction measures to meet interim emission targets. It is expected that the Province will ensure that an appropriate cost recovery mechanism is established to enable OPG to recover the costs of its coal-fired generating stations following the implementation of the CO<sub>2</sub> reductions.

On August 13, 2008, Standard & Poor's (S&P) announced that it raised OPG's long-term credit rating to "A-" with a stable outlook from "BBB+" with a positive outlook. At the same time, S&P affirmed OPG's "A-2" global scale and "A-1(Low)" Canada scale commercial paper rating. S&P stated that the upgrade in the long-term rating reflects a closer relationship between the company and its higher-rated owner, the Province (AA/Stable/A-1+), and a slightly stronger stand-alone credit profile, given the regulatory oversight of OPG's nuclear and baseload hydroelectric assets and an expected improvement in cash flow metrics.

The Portlands Energy Centre ("PEC") is a 550 MW high-efficiency, combined cycle, natural gas generation plant designed to meet downtown Toronto's urgent need for electricity. PEC is a limited partnership between OPG and TransCanada Energy Ltd. Construction of the station started in 2006 and the first phase was completed on schedule and on budget, in a simple cycle mode, with a capacity of up to 340 MW on May 31, 2008. In September 2008, the station will be taken out of service in order to complete construction of the combined cycle mode. PEC is expected to be completed and fully operational in the combined cycle configuration earlier than it's contractual in service date of June 1, 2009.

OPG's progress on a number of new generation projects aimed at significantly contributing to Ontario's long-term electricity supply requirements is as follows:

- At June 30, 2008, the boring machine for the Niagara tunnel had advanced 2,399 metres. The contractor previously advised OPG that due to excavation difficulties under the St. David's gorge, the in-service date of the tunnel will be delayed. To mitigate the impact of the schedule delay, the contractor continues to pursue alternatives including realignment of a portion of the tunnel. The project cost estimate of \$985 million will be reviewed in conjunction with any changes to the project completion schedule and the issues being considered in the ongoing dispute resolution process that is primarily focused on whether the actual subsurface rock conditions differ from the baseline established within the design-build contract.
- During the second quarter of 2008, the contractor advised OPG that completion of the 12.5 MW, Lac Seul generating station will be further delayed as a result of various contractor difficulties. These include the replacement by the contractor of the major subcontractor on two occasions, as well as delays related to cofferdam construction, intake construction and cofferdam removal. The expected in-service date for the new station will now be in the fourth quarter of 2008.
- In July 2008, OPG and the Ontario Power Authority executed a Hydroelectric Energy Supply Agreement for the Upper Mattagami and Hound Chute projects and continued negotiations regarding the Healey Falls project.
- On June 16, 2008, the Province announced that OPG will operate two new nuclear reactors at the Darlington site. OPG is proceeding with initiatives associated with the Environmental Impact Statement, which is planned for completion in early 2009. OPG is participating with Infrastructure Ontario in a process to select a nuclear reactor vendor. In addition, over the next several months, OPG plans to pursue cost recovery mechanisms and explore financing options for the new nuclear reactors.

## FINANCIAL AND OPERATIONAL HIGHLIGHTS

<i>(millions of dollars – except where noted)</i>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
<i>Earnings</i>				
Revenue after revenue limit rebate	1,385	1,373	2,948	2,897
Fuel expense	277	298	581	626
Gross margin	1,108	1,075	2,367	2,271
Operations, maintenance and administration	750	776	1,441	1,470
Other expenses	267	145	681	419
Income tax expenses (recoveries)	(8)	29	(16)	86
Net income	99	125	261	296
<i>Cash flow</i>				
Cash flow (used in) provided by operating activities	152	312	401	475
<i>Electricity Generation (TWh)</i>				
Regulated – Nuclear	10.1	11.1	23.4	22.7
Regulated – Hydroelectric	4.9	4.7	9.5	9.3
Unregulated – Hydroelectric	5.4	3.9	9.9	7.8
Unregulated – Fossil-Fuelled	5.5	6.3	12.5	14.4
Total electricity generation	25.9	26.0	55.3	54.2
<i>Average electricity sales price (¢/kWh)</i>				
Regulated – Nuclear <sup>1</sup>	4.9	4.9	4.9	4.9
Regulated – Hydroelectric <sup>1</sup>	3.6	3.5	3.6	3.6
Unregulated – Hydroelectric <sup>2</sup>	4.7	4.6	4.7	4.7
Unregulated – Fossil-Fuelled <sup>2</sup>	5.0	4.7	4.9	4.8
OPG average sales price	4.6	4.6	4.7	4.6
<i>Nuclear unit capability factor (per cent)</i>				
Darlington	80.7	84.4	89.8	88.9
Pickering A	63.3	61.6	70.5	62.5
Pickering B	57.3	72.2	71.9	70.9
<i>Equivalent forced outage rate (per cent)</i>				
Unregulated– Fossil-Fuelled	10.4	11.6	13.1	11.7
<i>Availability (per cent)</i>				
Regulated – Hydroelectric	93.2	93.2	93.4	92.6
Unregulated– Hydroelectric	97.6	95.4	96.6	95.2

<sup>1</sup> Electricity generated from stations in the Regulated – Hydroelectric segment received a fixed price of 3.3¢/kWh for the first 1,900 MWh of generation in any hour, and the Ontario spot electricity market price for generation above this level.

<sup>2</sup> Eighty-five per cent of the electricity generated from unregulated stations, excluding the Lennox generating station, those stations where generation output is subject to a Hydroelectric Energy Supply Agreement with the Ontario Power Authority, and forward sales as of January 1, 2005, is subject to a revenue limit. During the period from May 1, 2006 to April 30, 2007, the revenue limit was set at 4.6¢/kWh. The revenue limit increased to 4.7¢/kWh effective May 1, 2007 and to 4.8 ¢/kWh effective May 1, 2008.

Ontario Power Generation Inc. is an Ontario-based electricity generation company whose principal business is the generation and sale of electricity in Ontario. Our focus is on the efficient production and sale of electricity from our generation assets, while operating in a safe, open and environmentally responsible manner.

Ontario Power Generation Inc.'s unaudited interim consolidated financial statements and Management's Discussion and Analysis as at and for the three and six months ended June 30, 2008, can be accessed on OPG's website ([www.opg.com](http://www.opg.com)), the Canadian Securities Administrators' website ([www.sedar.com](http://www.sedar.com)), or can be requested from the Company.

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**2008 SECOND QUARTER REPORT**

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## **ONTARIO POWER GENERATION INC. MANAGEMENT'S DISCUSSION AND ANALYSIS**

This Management's Discussion and Analysis ("MD&A") should be read in conjunction with the unaudited interim consolidated financial statements and accompanying notes of Ontario Power Generation Inc. ("OPG" or the "Company") as at and for the three and six months ended June 30, 2008. For a complete description of OPG's corporate strategies, risk management, and the effect of critical accounting policies and estimates on OPG's results of operations and financial condition, this MD&A should also be read in conjunction with OPG's audited consolidated financial statements, accompanying notes, and MD&A as at and for the year ended December 31, 2007. Certain of the 2007 comparative amounts have been reclassified to conform to the 2008 presentation. OPG's consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and are presented in Canadian dollars. This MD&A is dated August 21, 2008.

### **FORWARD-LOOKING STATEMENTS**

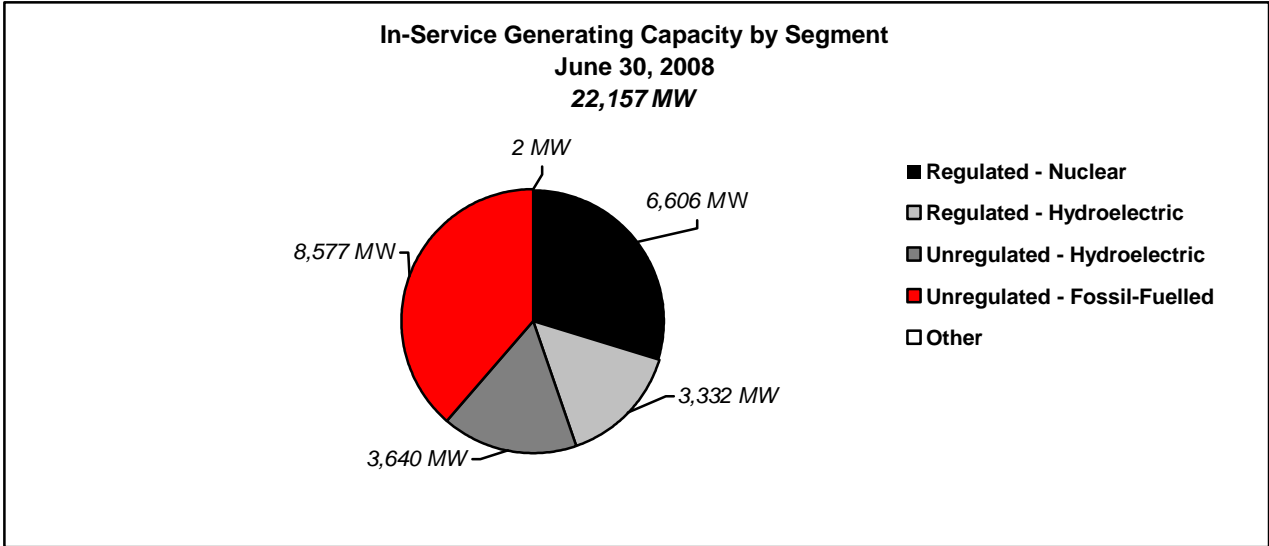
The MD&A contains forward-looking statements that reflect OPG's current views regarding certain future events and circumstances. Any statement contained in this document that is not current or historical is a forward-looking statement. OPG generally uses words such as "anticipate", "believe", "foresee", "forecast", "estimate", "expect", "schedule", "intend", "plan", "project", "seek", "target", "goal", "strategy", "may", "will", "should", "could" and other similar words and expressions to indicate forward-looking statements. The absence of any such word or expression does not indicate that a statement is not forward-looking.

All forward-looking statements involve inherent assumptions, risks and uncertainties and, therefore, could be inaccurate to a material degree. In particular, forward-looking statements may contain assumptions such as those relating to OPG's fuel costs and availability, asset performance, nuclear decommissioning and waste management, closure of coal-fired generating stations, refurbishment of existing facilities, development and construction of new facilities, pension and other post employment benefit obligations, income taxes, spot electricity market prices, the ongoing evolution of the Ontario electricity industry, environmental and other regulatory requirements, the weather, and the developments with respect to third-party Asset-Backed Commercial Paper. Accordingly, undue reliance should not be placed on any forward-looking statement. The forward-looking statements included in this MD&A are made only as of the date of this MD&A. OPG does not undertake to publicly update these forward-looking statements to reflect new information, future events or otherwise.

### **THE COMPANY**

OPG is an Ontario-based electricity generation company whose principal business is the generation and sale of electricity in Ontario. OPG's focus is on the efficient production and sale of electricity from its generating assets, while operating in a safe, open and environmentally responsible manner. OPG was established under the *Business Corporations Act* (Ontario) and is wholly owned by the Province of Ontario (the "Province").

At June 30, 2008, OPG's electricity generating portfolio had an in-service capacity of 22,157 megawatts ("MW"). OPG's electricity generating portfolio consists of three nuclear generating stations, five fossil-fuelled generating stations, 64 hydroelectric generating stations and two wind generating stations. In addition, OPG and TransCanada Energy Ltd. co-own the Portlands Energy Centre gas-fired generating station. OPG, ATCO Power Canada Ltd. and ATCO Resources Ltd. co-own the Brighton Beach gas-fired generating station. OPG also owns two other nuclear generating stations, which are leased on a long-term basis to Bruce Power L.P. ("Bruce Power").



**RATE REGULATION**

A regulation was introduced pursuant to the *Electricity Restructuring Act, 2004* (Ontario), which provides that, effective April 1, 2005, OPG receives regulated prices for electricity generated from most of its baseload hydroelectric and all of the nuclear facilities that it operates. This comprises electricity generated from the Sir Adam Beck 1, 2 and Pump generating station, DeCew Falls 1 and 2, and R.H. Saunders hydroelectric facilities, and Pickering A and B and Darlington nuclear facilities. The production from OPG’s other generating assets remains unregulated and continues to be sold at the Ontario electricity spot market price, subject to a revenue limit on the majority of this output.

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. OPG is seeking a rate of return consistent with the scope and type of business risks associated with safely and reliably operating, maintaining and developing its regulated assets.

In February 2008, the OEB held a hearing to consider OPG's request that payment amounts for its regulated facilities be declared interim, effective April 1, 2008, and OPG's request for an interim increase in payment amounts. The OEB granted OPG's request that payment amounts be made interim, effective April 1, 2008. This decision preserves the opportunity for OPG to recover the difference between final payment amounts as approved by the OEB and the current payment amounts, for the period between April 1, 2008 and the date of the OEB's final order. The decision regarding retrospective recovery will be made by the OEB as part of the final payment order. The OEB did not approve an interim increase in payment amounts. If a retrospective recovery adjustment is required, it can be achieved prospectively by spreading the impact of the adjustment over a period after the final order is made.

An oral hearing and arguments on OPG’s application were completed on August 5, 2008. The OEB’s final decision on the application is expected in the fall of 2008.



## HIGHLIGHTS

### Overview of Results

This section provides an overview of OPG's unaudited interim consolidated operating results. A detailed discussion of OPG's performance by reportable business segment is included under the heading, *Discussion of Operating Results by Business Segment*.

<i>(millions of dollars)</i>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
<i>Revenue</i>				
Revenue before revenue limit rebate	1,440	1,393	3,070	3,013
Revenue limit rebate	(55)	(20)	(122)	(116)
	1,385	1,373	2,948	2,897
<i>Earnings</i>				
Income before the following:	130	193	331	447
Other and losses	-	-	7	-
Income before interest and income taxes	130	193	324	447
Net interest expense	39	39	79	65
Income before income taxes	91	154	245	382
Income tax (recovery) expense	(8)	29	(16)	86
Net income	99	125	261	296
<i>Electricity production (TWh)</i>	25.9	26.0	55.3	54.2
<i>Cash flow</i>				
Cash flow (used in) provided by operating activities	152	312	401	475

Net income for the three months ended June 30, 2008 was \$99 million compared to net income of \$125 million for the same period in 2007, a decrease of \$26 million. Income before income taxes for the three months ended June 30, 2008 was \$91 million compared to income before income taxes during the same period in 2007 of \$154 million, a decrease of \$63 million.

Net income for the six months ended June 30, 2008 was \$261 million compared to \$296 million for the same period in 2007, a decrease of \$35 million. Income before income taxes for the six months ended June 30, 2008 was \$245 million compared to income before income taxes during the same period in 2007 of \$382 million, a decrease of \$137 million.

For the three and six months ended June 30, 2008, there was a net income tax recovery of \$8 million and \$16 million compared to an income tax expense of \$29 million and \$86 million for the same periods in the prior year. The decrease in the income tax expense was due to the impact of a reduction in income tax liabilities as a result of the resolution of the tax uncertainties related to the audit of OPG's 1999 taxation year during the first and second quarters of 2008.

The following is a summary of the factors impacting OPG's results for the three and six months ended June 30, 2008 compared to results for the same periods in 2007, on a before-tax basis:

<i>(millions of dollars – before tax)</i>	<b>Three Months</b>	<b>Six Months</b>
<b>Income before income taxes for the periods ended June 30, 2007</b>	<b>154</b>	<b>382</b>
Changes in gross margin		
Increase in electricity sales price after revenue limit rebate	19	23
Change in electricity generation by segment:		
Regulated – Nuclear	(43)	37
Regulated – Hydroelectric	4	4
Unregulated – Hydroelectric	64	91
Unregulated – Fossil-Fuelled	(19)	(37)
Increase (decrease) in ancillary revenue	10	(8)
Other changes in gross margin	(2)	(14)
	33	96
Increase in operations and maintenance expenses primarily due to higher costs for nuclear outage and maintenance activities, including advancement of fall outage work	(30)	(45)
Decrease in pension and other post employment benefit costs	15	31
Decrease in costs included in operations, maintenance and administration expenses related to past grievances by First Nations	41	43
Increase in accretion on fixed asset removal and nuclear waste management liabilities	(26)	(33)
Decrease in earnings from the nuclear fixed asset removal and nuclear waste management funds	(101)	(243)
Decrease in amortization of regulatory assets	16	23
Other changes	(11)	(2)
<b>Decrease in income before other gains and losses and income taxes</b>	<b>(63)</b>	<b>(130)</b>
Other gains and (losses) recognized in 2008	-	(7)
<b>Income before income taxes for the periods ended June 30, 2008</b>	<b>91</b>	<b>245</b>

#### *Earnings for the Three Months Ended June 30, 2008*

Earnings for the second quarter of 2008 were favourably impacted by an increase in gross margin from electricity sales compared to the same period in 2007 primarily due to higher generation from OPG's unregulated hydroelectric generating stations and a marginally higher electricity sales price, partially offset by lower generation from the nuclear and fossil-fuelled generating stations.

For the three months ended June 30, 2008, operations, maintenance and administration ("OM&A") expenses were \$750 million compared to \$776 million for the same period in 2007. The decrease was primarily due to a reduction in expenses related to the settlement of past grievances with First Nations, lower pension and other post employment benefit costs, and a reduction in planned outage work at the fossil-fuelled generating stations. The decrease was partly offset by higher costs at OPG's nuclear generating stations for maintenance activities and outage expenditures in the second quarter of 2008 compared to the same period in 2007.

Income for the three months ended June 30, 2008 was unfavourably impacted by a decrease in earnings on the nuclear fixed asset removal and nuclear waste management funds (the "Nuclear Funds") compared to the same period in 2007. Earnings on the Nuclear Funds for the three months ended June 30, 2008 were \$108 million compared to \$209 million for the same quarter in 2007, a decrease of \$101 million. The decrease in earnings was primarily due to lower returns on the Decommissioning Segregated Fund ("Decommissioning Fund") due to significant volatility and unfavourable returns in the

capital markets during the second quarter of 2008 compared to the same period in 2007. The Nuclear Funds are invested to fund long-term liability requirements and as such, the portfolio asset mix is structured to achieve the required return over a long-term horizon. While short-term market fluctuations will occur, managing the Decommissioning Fund investments to meet the Fund's long-term target return remains the primary goal. In addition, during the second quarter of 2007, the earnings on the Decommissioning Fund were favourably impacted by a \$46 million reimbursement for expenditures related to the safe storage of Pickering A Units 2 and 3.

OPG's earnings on the Used Fuel Segregated Fund ("Used Fuel Fund") are not subject to such capital market volatility since the rate of return on this fund is guaranteed by the Province for the first 2.23 million used fuel bundles.

OPG is in the process of seeking new payment amounts for its regulated facilities effective April 1, 2008. Pending the OEB's final decision, OPG has changed its method of accounting for certain deferral accounts. Specifically, OPG has changed its amortization of the Pickering A return to service deferral account consistent with the method proposed in the rate application. OPG has also discontinued the deferral of costs associated with increases in OPG's liabilities for nuclear used fuel management and nuclear decommissioning and low and intermediate level waste management arising from the 2006 Approved Reference Plan, and costs associated with new nuclear generation development.

#### *Earnings for the Six Months Ended June 30, 2008*

Earnings for the six months ended June 30, 2008 compared to the same period in 2007 were favourably impacted by an increase in gross margin largely due to higher generation from OPG's unregulated hydroelectric stations and the nuclear generating stations. Lower generation from the fossil-fuelled generating stations had an unfavourable impact on gross margin.

Income for the six months ended June 30, 2008 was significantly impacted by a decrease in earnings from the Nuclear Funds of \$243 million compared to the same period in 2007. The decrease was due to continued market volatility and unfavourable returns in the capital markets, and the reimbursement during the second quarter of 2007 for expenditures related to the safe storage of Pickering A Units 2 and 3.

For the six months ended June 30, 2008, OM&A expenses were \$1,441 million compared to \$1,470 million for the same period in 2007. The decrease was primarily due to a reduction in expenses related to past grievances by First Nations, lower pension and other post employment benefit costs, and a reduction in planned outage work for the fossil-fuelled generating stations. The decrease was partly offset by higher costs at OPG's nuclear generating stations for maintenance activities and outage expenditures during the six months ended June 30, 2008 compared to the same period in 2007.

## Average Sales Prices

The weighted average Ontario spot electricity market price and OPG's average sales prices by reportable business segment, net of the revenue limit rebate for the three and six months ended June 30, 2008 and 2007, were as follows:

<i>(¢/kWh)</i>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Weighted average hourly Ontario spot electricity market price	5.0	4.6	5.1	5.0
Regulated – Nuclear	4.9	4.9	4.9	4.9
Regulated – Hydroelectric <sup>1</sup>	3.6	3.5	3.6	3.6
Unregulated – Hydroelectric <sup>2</sup>	4.7	4.6	4.7	4.7
Unregulated – Fossil-Fuelled <sup>2</sup>	5.0	4.7	4.9	4.8
OPG's average sales price	4.6	4.6	4.7	4.6

<sup>1</sup> Electricity generated from stations in the Regulated – Hydroelectric segment received a fixed price of 3.3¢/kWh for the first 1,900 MWh of generation in any hour, and the Ontario spot electricity market price for generation above this level.

<sup>2</sup> 85 per cent of the electricity generated from unregulated stations, excluding the Lennox generating station, those stations where generation output is subject to a Hydroelectric Energy Supply Agreement ("HESA") with the Ontario Power Authority, and forward sales as of January 1, 2005, is subject to a revenue limit. During the period from May 1, 2006 to April 30, 2007, the revenue limit was set at 4.6¢/kWh. The revenue limit increased to 4.7¢/kWh effective May 1, 2007 and to 4.8 ¢/kWh effective May 1, 2008.

The weighted average hourly Ontario spot electricity market price was 5.0¢/kWh for the three months ended June 30, 2008 compared to 4.6¢/kWh for the same period in 2007. The weighted average hourly Ontario spot electricity market price was 5.1¢/kWh for the six months ended June 30, 2008 compared to 5.0 ¢/kWh for the same period in 2007. The increase was primarily due to higher coal and natural gas market prices, partially offset by the impact of higher hydroelectric generation and a stronger Canadian dollar, which contribute to lower spot market prices.

The increase in OPG's average sales price from the Unregulated – Hydroelectric and Unregulated – Fossil-Fuelled segments for the three months ended June 30, 2008 compared to the same period in 2007 reflected the impact of higher Ontario spot market prices and a higher revenue limit in 2008.

OPG's average sales price for the three and six month period ended June 30, 2008 and 2007 was at or lower than the weighted average hourly Ontario spot electricity market price as a result of regulated prices and the revenue limit rebate.

## Electricity Generation

Total electricity generated during the three months ended June 30, 2008 from OPG's generating stations was 25.9 TWh compared to 26.0 TWh during the same period in 2007. The decrease was primarily due to lower generation from the nuclear and fossil-fuelled generating stations, largely offset by higher electricity generation from OPG's unregulated hydroelectric facilities.

Electricity generation from the nuclear generating stations during the three months ended June 30, 2008 was 10.1 TWh compared to 11.1 TWh during the same period in 2007. The decrease in generation was primarily due to an increase in outage days at the Pickering B nuclear generating station.

For the three month periods ended June 30, 2008 and 2007, electricity sales volume from the Regulated – Hydroelectric segment was 4.9 TWh and 4.7 TWh, respectively. Electricity generated from the unregulated hydroelectric generating stations during the second quarter of 2008 was 5.4 TWh compared to 3.9 TWh during the same period in 2007. The increase was primarily due to higher river flows across the province.

Electricity generation from the fossil-fuelled generating stations was 5.5 TWh in the second quarter of 2008 compared to 6.3 TWh in the second quarter of 2007. The decrease was primarily due to higher generation from the hydroelectric generating stations.

For the six months ended June 30, 2008, total electricity generated from OPG's generating stations was 55.3 TWh compared to 54.2 TWh during the same period in 2007. The increase was primarily due to higher generation from the unregulated hydroelectric and nuclear generating stations, partly offset by a decrease in generation from the fossil-fuelled generating stations.

During the six months ended June 30, 2008, electricity generation from the nuclear generating stations was 23.4 TWh compared to 22.7 TWh for the same period in 2007. The 0.7 TWh increase was primarily due to outages during the first half of 2007 at the Pickering nuclear generating stations that reduced generation compared to the same period in 2008, and continued strong performance at the Darlington nuclear generating station.

For the six months ended June 30, 2008, electricity sales volume from the Regulated – Hydroelectric segment was 9.5 TWh compared to 9.3 TWh in the same period in 2007. Electricity generated from the unregulated hydroelectric generating stations during the six months ended June 30, 2008 was 9.9 TWh compared to 7.8 TWh during the same period in 2007, an increase of 2.1 TWh. The increase was primarily due to higher river flows across the province.

Electricity generation from OPG's fossil-fuelled generating stations for the six months ended June 30, 2008 was 12.5 TWh compared to 14.4 TWh during the same period in 2007. The decrease in generation was primarily due to higher generation from OPG's hydroelectric and nuclear generating stations.

OPG's operating results are impacted by changes in demand resulting from variations in seasonal weather conditions. The following table provides a comparison of Heating and Cooling Degree Days for the three and six months ended June 30:

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Heating Degree Days <sup>1</sup>				
Period	467	500	2,360	2,420
Ten-year average	497	490	2,355	2,320
Cooling Degree Days <sup>2</sup>				
Period	75	127	75	127
Ten-year average	91	95	91	95

<sup>1</sup> Heating Degree Days are recorded on days with an average temperature below 18°C, and represent the aggregate of the differences between the average temperature and 18°C for each day during the period, as measured at Pearson International Airport in Toronto, Ontario.

<sup>2</sup> Cooling Degree Days are recorded on days with an average temperature above 18°C, and represent the aggregate of the differences between the average temperature and 18°C for each day during the period, as measured at Pearson International Airport in Toronto, Ontario.

Heating Degree Days decreased for the three months ended June 30, 2008 compared to the same period in 2007 due to mild weather conditions. Ontario primary electricity demand was 35.1 TWh and 36.3 TWh for the three months ended June 30, 2008 and 2007, respectively.

Heating Degree Days decreased for the six months ended June 30, 2008 compared to the same period in 2007. Temperature during the six months ended June 30, 2008 approximated the ten-year average. Ontario primary electricity demand was 74.6 TWh and 76.3 TWh for the six months ended June 30, 2008 and 2007, respectively.

## **Recent Developments**

### *New Nuclear Generating Units*

As directed by the Minister of Energy in June 2006, OPG initiated a federal approvals process by filing an Application for a Site Preparation Licence with the CNSC for new nuclear generating units at the Darlington nuclear generating site. In January 2008, the CNSC recommended to the Federal Minister of Environment that the project be referred to a panel review, which is the highest level of review under current legislation. In March 2008, the recommendation was accepted and the project Environmental Assessment ("EA") was referred to a review panel. Work continues on the Environmental Impact Statement, which is planned for completion in early 2009.

In March 2008, the Minister of Energy announced a two-phase competitive Request For Proposal ("RFP") process to select a nuclear reactor vendor for two units of baseload generation to provide 2,000 to 3,500 MW of generation capacity to the Ontario electricity grid. The target in-service date as stated by Infrastructure Ontario is mid-2018 for the first unit and mid-2019 for the second unit. A commercial team, directed by Infrastructure Ontario and supported by OPG, Bruce Power, and the Ministries of Energy and Infrastructure and Finance, is managing the procurement process to select a nuclear reactor vendor by the end of March 2009.

Phase one of the RFP process was aimed at assessing the ability of the invited vendors to support a successful construction licence application in compliance with Canadian regulatory requirements and to successfully deliver the overall project, as well as to ascertain their financial strength and legal position. Phase one was completed in June 2008 with Areva NP, Atomic Energy of Canada Limited, and Westinghouse advancing to phase two.

Phase two of the competitive RFP process was launched on June 16, 2008 to select a nuclear reactor vendor. The competitive process is to select a vendor to develop, construct, and provide licensing, commissioning and engineering, operations and maintenance support and fuel supply, and possibly financing, of a stand-alone two-unit nuclear power plant at the Darlington site. Respondents will be evaluated in three key areas: lifetime cost of power, ability to meet Ontario's timetable to bring new supply on line in 2018, and level of investment in Ontario. The deadline for Phase two final proposal submissions has recently been extended by three months to December 31, 2008, in response to a request from the vendors to allow for more discussion on the appropriate risk transfer and pricing terms, and to ensure the provision of quality bids. Selection of the preferred vendor has also been deferred by three months to the end of March 2009. A number of meetings were held with the three vendors to solicit feedback on the technical and commercial aspects of the draft Project Agreement. Additional meetings are planned throughout the remainder of Phase two.

On June 16, 2008, the Province announced that two new nuclear reactors for Ontario would be located at the Darlington site and that OPG had been selected as the operator for the units. Over the next several months, OPG will focus on supporting the vendor selection process, pursuing cost recovery mechanisms and exploring financing options.

### *Long-Term Credit Rating*

On August 13, 2008, Standard & Poor's (S&P) raised OPG's long-term credit rating to "A-" with a stable outlook from "BBB+" with a positive outlook. At the same time, S&P affirmed OPG's "A-2" global scale and "A-1(Low)" Canada scale commercial paper rating. S&P stated that the upgrade in the long-term rating reflects a closer relationship between the company and its higher-rated owner, the Province (AA/Stable/A-1+), and a slightly stronger stand-alone credit profile, given the regulatory support and an expected improvement in cash flow metrics. S&P added that regulatory oversight of the company's baseload nuclear and hydroelectric assets, a diverse generation portfolio, and a cost-competitive position, support OPG's strong business risk profile.

### *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. The total face value of affected ABCP amounted to \$32 billion. 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 gains and losses. OPG's remaining holdings of third party ABCP are recorded as long-term investments.

The remaining investment 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. The sanctioning of the Plan by the Ontario Superior Court was delayed until June 2008, to incorporate certain amendments to the Plan. Despite the ruling of the Ontario Superior Court, a motion by a number of noteholders opposing the sanctioning of the Plan went before the Ontario Court of Appeal. In August 2008, the Ontario Court of Appeal upheld the earlier decision of the Ontario Superior Court. Absent a further appeal to the Supreme Court of Canada by noteholders who objected to the restructuring, the committee of large noteholders expects the Plan to close by September 30, 2008. OPG continues to monitor events related to the Plan and its implementation.

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.

### *Climate Change Plan*

The Federal Government, in April 2007, announced targets for reducing both greenhouse gas ("GHG") emissions and air pollutants from 2006 levels. Under the Federal proposal, OPG would be required to reduce its intensity levels of GHG emissions from its fossil-fuelled generating stations from 2006 levels by 18 per cent in 2010, with an eventual reduction of 26 per cent by 2015. The Federal Government confirmed these GHG targets in March 2008. The Federal Government also confirmed that for the electricity sector, GHG intensity would be calculated at the corporate level, rather than at the station or fleet levels. The Federal Government plans to release the draft GHG regulations as well as a regulatory framework for air pollutants in the fall of 2008.

In May 2008, the Province announced new annual limits on CO<sub>2</sub> emissions from OPG's coal-fired generating stations to ensure that such emissions are reduced by two-thirds of the 2003 levels by 2011. A draft regulation under the Environmental Protection Act requires a reduction in CO<sub>2</sub> emissions to an annual limit of 11.5 million tonnes beginning on January 1, 2011, one third of the 34.5 million tonnes of CO<sub>2</sub> emissions produced in 2003. In accordance with the May 15, 2008 Shareholder Declaration and the May 16, 2008 Shareholder Resolution, OPG is required to stage the reduction measures to meet on a forecast basis the interim CO<sub>2</sub> emission targets of 19.6 million tonnes in 2009 and 15.6 million tonnes in 2010. OPG is required to submit a strategy outlining how it will achieve these objectives to the Minister of Energy by November 30, 2008, for the 2009 calendar year, and within one year thereafter for 2010. These strategies may result in a reduction to OPG's revenues. It is expected that the Province will ensure that an appropriate cost recovery mechanism is established to enable OPG to recover the costs of its coal-fired generating stations following the implementation of the CO<sub>2</sub> reductions.

## **VISION, CORE BUSINESS AND STRATEGY**

OPG's mandate is to cost effectively produce electricity from its diversified generating assets, while operating in a safe, open and environmentally responsible manner. To achieve its mandate, OPG is focused on four corporate strategies: improving the performance of its generating assets; increasing its generating capacity; achieving financial sustainability; and achieving excellence in corporate governance, safety, social responsibility, corporate citizenship and environmental stewardship.

A detailed discussion of OPG's strategies is outlined in the 2007 annual MD&A under the heading, *Vision, Core Business and Strategy*. The following section provides an update to the year end discussion.

## **Improving the Performance of Generating Assets**

### *Nuclear Generating Assets*

#### Refurbishment Projects

Work is proceeding on the feasibility study to refurbish the Pickering B nuclear generating station. This includes an assessment of the station condition, an EA, and an Integrated Safety Review ("ISR"), which is designed to ensure safe and secure operations of the generating station for the proposed future period. OPG submitted a draft Environment Impact Study report to the Canadian Nuclear Safety Commission ("CNSC") in December 2007. The CNSC staff accepted the Environmental Assessment Study Report and held open houses on their draft EA Screening Report, which was issued in July 2008.

Preparatory work for the feasibility study on the refurbishment of the Darlington nuclear generating station began in the first quarter of 2008. The scope definition for the Darlington Refurbishment project has been finalized. The current Darlington Refurbishment project work includes an ISR and an assessment of plant condition. The overall plant condition assessment was started in the second quarter of 2008. A third-party assessment on the condition of the steam generators is underway and is expected to be completed in the fall of 2008. The Darlington "ISR Basis Document" is also under development.

#### Pickering A Units 2 and 3 Safe Storage Project

The Pickering A safe storage project includes isolating Units 2 and 3 from the rest of the generating station, redesigning the control room for the remaining two operating units, and de-watering and de-fuelling the units. De-fuelling of Unit 2 is completed and the de-fuelling for Unit 3 is progressing.

In the third quarter of 2007, the CNSC concluded that an EA was necessary for certain aspects of the safe storage project and therefore certain planned work was suspended pending the completion of the EA. As a result of the EA requirement, the completion of the project is now scheduled for the fall of 2010 and total project costs are estimated to be \$350 million. Work continues in areas not constrained by the EA.

## **Increasing OPG's Generating Capacity**

### Niagara Tunnel

At June 30, 2008, the tunnel boring machine had advanced 2,399 metres. The progress of the tunnel boring machine by the design build contractor has been much slower than expected through rock conditions encountered under the St. David's gorge. Progress of the tunnel boring machine has recently increased since completion of the excavation under the St. David's gorge.

The contractor previously advised OPG that the in-service date of the tunnel would be delayed. The contract structure places the onus on the contractor to investigate schedule delays and includes liquidated damages provisions for failure to meet the contracted in-service date. To mitigate the impact of the schedule delay, the contractor is continuing to pursue alternatives, including realignment of a portion of the tunnel. OPG is taking steps to acquire subsurface property rights required to facilitate a potential realignment.

The estimated in-service date will be dependent on whether the contractor decides to implement an alternative approach. Regardless of the approach pursued by the contractor, considerable uncertainty remains with respect to the schedule until the tunnel boring machine establishes consistent tunneling performance beyond the St. David's gorge.



The project cost estimate of \$985 million will be reviewed in conjunction with any changes to the project completion schedule and the results of a dispute review board hearing. The dispute review hearing process was initiated to review, among other things, the actual subsurface conditions compared to those that were anticipated as part of the design build contract. The hearing was held during the week of June 23, 2008. The dispute review board is expected to issue its non-binding recommendations prior to September 30, 2008. The schedule delay and the issues currently being considered by the dispute review board could impact the project cost.

The capital project expenditures for the three months ended June 30, 2008 were \$19 million and life-to-date capital expenditures were \$345 million. The project is debt financed through the Ontario Electricity Financial Corporation ("OEFC").

#### *Lac Seul*

The Lac Seul generating station was expected to be in-service by the end of the third quarter of 2007 in accordance with the original schedule set out in the design-build contract between OPG and the contractor. However, the project has been delayed as a result of various contractor difficulties, including the replacement by the contractor of its major civil subcontractor on two occasions, as well as delays related to intake construction, and cofferdam construction and removal. The contractor has advised OPG that the expected in-service date for the new station will now be in the fourth quarter of 2008.

The design-build contract includes liquidated damages terms to mitigate, among other things, the impact to OPG of a schedule delay. OPG is deducting applicable liquidated damages from amounts otherwise payable to the contractor for the late in-service date. There is a possibility that the contractor may file a claim against OPG seeking recovery of certain additional costs related to the schedule delays.

Life-to-date expenditures were \$46 million. Total project cost is expected to be \$47 million, net of the recovery of liquidated damages, which is subject to change in the event the contractor successfully validates its right to additional costs related to schedule delays. The project is debt financed through the OEFC.

#### *Upper Mattagami and Hound Chute*

In December 2007, OPG's Board of Directors approved the redevelopment of four existing hydroelectric generating stations. Three of the generating stations are on the Upper Mattagami River (Wawaitin, Sandy Falls and Lower Sturgeon) and the fourth (Hound Chute) is located on the Montreal River. The project includes the demolition and decommissioning of the four existing powerhouses, that are at the end of their useful lives, and the rehabilitation of the existing dams and other civil structures to meet the current Dam Safety Requirements. Upon completion of the project, the total installed capacity of the four stations will increase from 23 MW to 44 MW, and the annual energy will increase from 134 gigawatt hours ("GWh") to 223 GWh.

Total project costs are expected to be \$300 million. A significant proportion of this capital cost relates to a design-build contract to construct the facilities.

#### *Lower Mattagami*

Following discussions with the Canadian Environmental Assessment Agency ("CEAA"), it was determined that a comprehensive study process must be followed under CEAA regulations. The CEAA is in the process of obtaining ministerial approval for this decision. OPG is in the process of identifying vendors to which request for proposals for a design build contract will be issued.

#### *Hydroelectric Projects Directive*

In December 2007, the Minister of Energy issued a directive to the Ontario Power Authority ("OPA") to negotiate Hydroelectric Energy Supply Agreements ("HESA") for the Lac Seul, Upper Mattagami, Hound Chute, Healey Falls and Lower Mattagami projects. The Lac Seul HESA has been executed. The HESA

for the Upper Mattagami and Hound Chute was approved by the OPA in July 2008. The negotiations for the HESA for the Healey Falls project are in progress.

#### *Portlands Energy Centre*

In May 2008, the construction for the simple cycle mode of operations for the Portland Energy Centre ("PEC") was completed. Under the simple cycle mode, PEC has a generating capacity of up to 340 MW. The work to complete the simple cycle mode of operations was completed on schedule and within the approved budget.

The station will operate in a simple cycle mode as needed during the summer and will be taken out of service at the end of September 2008 to complete the construction for a combined cycle mode of operation. Considerable work is in progress for the combined cycle mode. PEC is expected to be completed and fully operational in the combined cycle configuration earlier than its contractual in-service date of June 1, 2009, and will provide up to 550 MW of power.

OPG's share of capital expenditures for the three months ended June 30, 2008 was \$22 million. Total project costs continue to be within the \$730 million approved budget, excluding capitalized interest. A significant proportion of this capital cost relates to an engineer-procure-construct contract to construct the facility. OPG's share of the project is debt financed through the OEFC.

#### *Lakeview Site*

In July 2008, the Ontario government announced that the Lakeview site will not be used for a new gas-fired generating station.

### **ONTARIO ELECTRICITY MARKET TRENDS**

In its 18-Month Outlook published in June 2008, the IESO indicated that Ontario's installed electricity generating capacity was 31,642 MW, an increase from the previously reported capacity on April 1, 2008 of 31,297 MW. The capacity increase includes the addition of the PEC simple cycle operation in June 2008. The IESO reported that the supply picture is expected to change significantly over the next 18 months. About 4,300 MW of new supply is scheduled to come online or return to service, including approximately 2,800 MW of gas fired generation, 800 MW of nuclear generation, 100 MW of hydroelectric generation and about 600 MW of wind capacity. Ontario's import capability will increase by about 30 per cent with the new 1,250 MW interconnection between Ontario and Quebec, scheduled to be completed by next spring. The expected peak electricity demand in the summer of 2008, under normal weather conditions, is forecast by the IESO to be 25,232 MW. The IESO expects energy demand in 2008 to decrease by 1 per cent to 150.0 TWh, with a further 1.1 per cent decrease in 2009 to 148.3 TWh. The decrease in demand forecast is primarily attributed to lower industrial demand and increased conservation measures. The IESO reported that over the next 18 months, the outlook for Ontario's supply/demand balance is generally positive and improving. OPG's in-service electricity generating capacity as at June 30, 2008 was 22,157 MW or 70 per cent of Ontario's capacity.

Both the spot electricity market price and fuel prices can have a significant impact on OPG's revenue and gross margin. Uranium market prices increased significantly beginning in 2003. Spot prices peaked in May 2007 and have since declined to levels which are still significantly above pre-2003 levels. Near-term impact on OPG's nuclear fuel costs has been mitigated by existing lower priced long-term supply agreements and the consumption of low-cost inventory. However, fuel costs for nuclear operations are expected to be significantly higher in the future. Average market prices during the second quarter of 2008 for natural gas increased by approximately 50 per cent and coal prices increased approximately 100 per cent compared to average prices over the same period in 2007. The outlook for gas prices remains volatile through the summer as high oil prices, seasonally-low working-gas storage levels and threats for storm-related disruptions through hurricane season are expected to keep prices firm. Coal prices have been driven by a relatively low US dollar, high global demand for steam and metallurgical coal and overall pressure on supplies.

## KEY GENERATION AND FINANCIAL PERFORMANCE INDICATORS

Key performance indicators that directly pertain to OPG's mandate and corporate strategies are measures of production efficiency, cost effectiveness, and environmental performance. OPG evaluates the performance of its generating stations using a number of key performance indicators, which vary depending on the generating technology. These indicators are defined in the 2007 annual MD&A and are discussed in the *Discussion of Operating Results by Business Segment* section.

## DISCUSSION OF OPERATING RESULTS BY BUSINESS SEGMENT

This section summarizes OPG's key results by segment for the three and six months ended June 30, 2008 and 2007. The following table provides a summary of revenue, earnings and key generation and financial performance indicators by business segment:

<i>(millions of dollars)</i>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
<i>Revenue, net of revenue limit rebate</i>				
Regulated – Nuclear	593	632	1,358	1,314
Regulated – Hydroelectric	191	179	369	355
Unregulated – Hydroelectric	279	196	499	387
Unregulated – Fossil-Fuelled	307	326	685	774
Other	15	40	37	67
	1,385	1,373	2,948	2,897
<i>Income (loss) before interest and income taxes</i>				
Regulated – Nuclear	(132)	65	(191)	54
Regulated – Hydroelectric	81	41	167	121
Unregulated – Hydroelectric	182	98	314	206
Unregulated – Fossil-Fuelled	(2)	(34)	35	33
Other	1	23	(1)	33
	130	193	324	447
<i>Electricity Generation (TWh)</i>				
Regulated – Nuclear	10.1	11.1	23.4	22.7
Regulated – Hydroelectric	4.9	4.7	9.5	9.3
Unregulated – Hydroelectric	5.4	3.9	9.9	7.8
Unregulated – Fossil-Fuelled	5.5	6.3	12.5	14.4
Total electricity generation	25.9	26.0	55.3	54.2
<i>Nuclear unit capability factor (per cent)</i>				
Darlington	80.7	84.4	89.8	88.9
Pickering A	63.3	61.6	70.5	62.5
Pickering B	57.3	72.2	71.9	70.9
<i>Equivalent forced outage rate (per cent)</i>				
Regulated – Hydroelectric	1.1	0.7	1.4	1.0
Unregulated – Hydroelectric	0.7	1.4	0.6	1.3
Unregulated – Fossil-Fuelled	10.4	11.6	13.1	11.7
<i>Availability (per cent)</i>				
Regulated – Hydroelectric	93.2	93.2	93.4	92.6
Unregulated – Hydroelectric	97.6	95.4	96.6	95.2
<i>Nuclear PUEC (\$/MWh)</i>	54.23	47.23	45.88	45.46
<i>Regulated – Hydroelectric OM&amp;A expense per MWh (\$/MWh)</i>	4.90	5.11	5.05	5.05
<i>Unregulated – Hydroelectric OM&amp;A expense per MWh (\$/MWh)</i>	8.33	11.28	9.09	10.77
<i>Unregulated – Fossil-Fuelled OM&amp;A expense per MW (\$000/MW)</i>	63.0	71.9	59.7	66.3

## Regulated – Nuclear Segment

<i>(millions of dollars)</i>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Regulated generation sales	499	545	1,153	1,114
Other	94	87	205	200
Total revenue	593	632	1,358	1,314
Fuel expense	36	33	77	65
Gross margin	557	599	1,281	1,249
Operations, maintenance and administration	542	510	1,042	1,009
Depreciation and amortization	95	100	201	216
Accretion on fixed asset removal and nuclear waste management liabilities	150	124	283	250
Earnings on nuclear fixed asset removal and nuclear waste management funds	(108)	(209)	(57)	(300)
Property and capital taxes	10	9	3	20
Income before interest and income taxes	(132)	65	(191)	54

### Revenue

Regulated – Nuclear revenue was \$593 million for the three months ended June 30, 2008 compared to \$632 million for the same quarter in 2007. The decrease in revenue of \$39 million was primarily due to lower generation of 1.0 TWh during the second quarter of 2008 compared to the same period last year.

Regulated – Nuclear revenue for the six months ended June 30, 2008 and 2007, was \$1,358 million and \$1,314 million, respectively. The increase in revenue of \$44 million was primarily due to higher generation of 0.7 TWh in the first six months of 2008 compared to the same period in 2007.

### Electricity Prices

Electricity generation from stations in the Regulated – Nuclear segment received a fixed price of 4.95¢/kWh since the introduction of rate regulation effective April 1, 2005.

### Volume

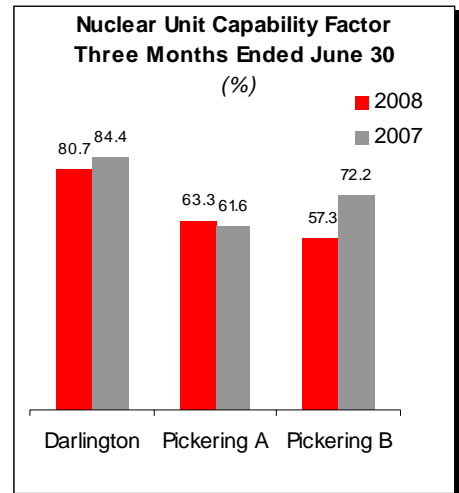
Electricity generation from OPG's nuclear stations was 10.1 TWh for the second quarter of 2008 compared to 11.1 TWh for the same period in 2007. The decrease of 1.0 TWh was primarily due to an extended unplanned outage at the Pickering B nuclear generating station to replace a calandria tube. Nuclear generation in the second quarter of 2008 was also impacted by an unplanned outage at the Pickering A nuclear generating station to conduct repairs on a fuel handling machine. Nuclear generation in 2007 was impacted by the shutdown of the Pickering A nuclear generating station Units 1 and 4 in early June 2007 to perform modifications on a backup electrical system.

Nuclear generation for the six month period ended June 30, 2008 was 23.4 TWh compared to 22.7 TWh for the same period in 2007. The increase of 0.7 TWh was primarily due to outages during the first six months of 2007 at the Pickering nuclear generating stations that reduced generation compared to the first half of 2008, and continued strong performance at the Darlington nuclear generating station. The generation during the first six months of 2007 was impacted by an unplanned outage at the Pickering B generating station caused by an inadvertent release of resin by a third-party contractor from the water treatment plant into the station's demineralized water system, and the requirement for maintenance related to the recovery of resin. Generation during the first quarter of 2007 was also impacted by an extension to a planned outage at the Pickering A nuclear generating station for significant additional repair work required as a result of a component failure during inspection.

The Darlington nuclear generating station's unit capability factor for the three months ended June 30, 2008 was 80.7 per cent compared to 84.4 per cent for the same period in 2007. The decrease in the capability factor reflects the higher planned outage days in the second quarter of 2008 compared to the same period in 2007.

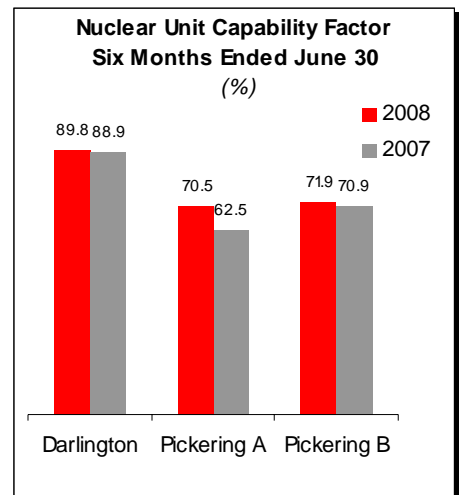
The unit capability factor for the Pickering A nuclear generating station for the three months ended June 30, 2008 was 63.3 per cent compared to 61.6 per cent in 2007. The unit capability factor for the three months ended June 30, 2008 was impacted by an unplanned outage to conduct repairs on a fuel handling machine. For the three months ended June 30, 2007, the unit capability factor reflected the shutdown of Units 1 and 4 in June 2007 to perform modifications on a backup electrical system.

The unit capability factor for the Pickering B nuclear generating station was 57.3 per cent for the three months ended June 30, 2008 compared to 72.2 per cent for same quarter in 2007. The decrease primarily reflects the shutdown of a unit to replace a calandria tube and an extension to a planned outage.



For the six months ended June 30, 2008, the unit capability factor for the Darlington nuclear generating station was 89.8 per cent compared to 88.9 per cent for the same period in 2007. The increase was due to a lower number of planned outage days at the Darlington nuclear generating station in 2008 compared to the same period in 2007. The unit capability factors reflect the continuing high performance of the Darlington station.

The Pickering A nuclear generating station's unit capability factor was 70.5 per cent for the six months ended June 30, 2008 compared to 62.5 per cent during the same period in 2007. The increase was primarily due to the shutdown of Units 1 and 4 in June 2007 and an extension to a planned outage for significant additional repair work required as a result of a component failure during inspection in the first quarter of 2007, partially offset by the impact of an unplanned outage in 2008.



For the six months ended June 30, 2008, the Pickering B nuclear generating station unit capability factor was 71.9 per cent compared to 70.9 per cent during the same period in 2007. The unit capability factor for the six months ended June 30, 2008 was impacted by the shutdown of a unit to replace a calandria tube and an extension to a planned outage. During the first half of 2007, the unit capability factor for the Pickering B generating station was impacted by an unplanned outage related to the release of resin into the demineralized water system.

#### *Fuel Expense*

Fuel expense for the three months ended June 30, 2008 was \$36 million compared to \$33 million during the same period in 2007. The increase in fuel expense was primarily due to higher uranium prices.

For the six months ended June 30, 2008, fuel expense was \$77 million compared to \$65 million during the same period in 2007. The increase in fuel expense was primarily due to higher uranium prices and higher generation volume.

### Operations, Maintenance and Administration

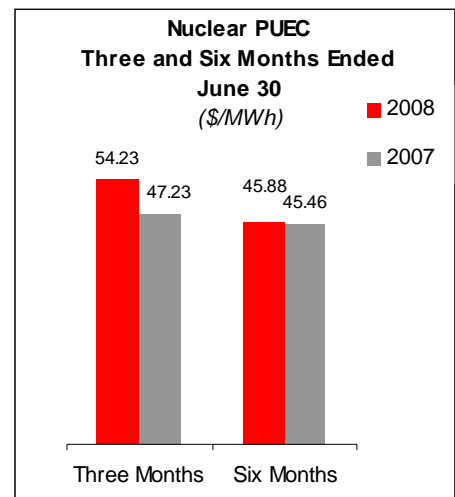
OM&A expenses for the three months ended June 30, 2008 were \$542 million compared to \$510 million during the same period in 2007. OM&A expenses were \$1,042 million for the six months ended June 30, 2008 compared to \$1,009 million during the same period in 2007. The increase in OM&A expenses was primarily due to higher costs for outage and maintenance activities and the advancement of fall outage work at the Pickering B generating station. The increase in OM&A expenses was partially offset by a reduction in pension and other post employment benefit costs.

Based on amendments to the regulation pursuant to the *Electricity Restructuring Act, 2004* (Ontario) made in February 2007 and February 2008, OPG recorded a regulatory asset related to non-capital costs for nuclear generation development initiatives. 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. Non-capital costs for nuclear generation development initiatives of \$11 million are included in OM&A expenses for the three months ended June 30, 2008. In the three months ended June 30, 2007, OPG recorded as a regulatory asset, \$5 million of non-capital costs for nuclear generation development initiatives pursuant to the regulation. The amendment to the regulation which was made in February 2008, also instructs OPG to establish a variance account, as of the effective date of the OEB’s order, to record the differences between actual costs associated with new nuclear generation development and the amount included in OPG’s forecast for purposes of establishing new payment amounts. OPG will start recording costs in the variance account based on the effective date of the OEB’s payment order expected to be issued in the fall of 2008.

For the three months ended March 31, 2008, OPG recorded a regulatory asset of \$4 million for non-capital costs for nuclear generation development initiatives. During the six months ended June 30, 2007, OPG recorded \$14 million as a regulatory asset.

Nuclear PUEC for the three months ended June 30, 2008 was \$54.23/MWh compared to \$47.23/MWh during the same period in 2007. The increase was primarily due to lower generation and higher OM&A expenses for the second quarter of 2008.

Nuclear PUEC for the six months ended June 30, 2008 was \$45.88/MWh compared to \$45.46/MWh during the same period in 2007. The increase was primarily due to higher OM&A expenses, partially offset by higher generation.



### Depreciation and Amortization

Depreciation and amortization expense for the three months ended June 30, 2008 was \$95 million compared to \$100 million for the same period in 2007. For the six months ended June 30, 2008, depreciation and amortization expense was \$201 million compared to \$216 million during the six months ended June 30, 2007. The decrease in depreciation and amortization expense was primarily due to a lower amortization of the Pickering A return to service deferral account.

Effective April 1, 2008, OPG changed the method of amortization of the Pickering A return to service deferral account to align with the method proposed in the rate application. Amortization for the three months ended June 30, 2008 was \$4 million compared to \$20 million during the three months ended June 30, 2007. For the six months ended June 30, 2008 and 2007, amortization was \$33 million and \$56 million, respectively.

### Accretion

Accretion expense for the three months ended June 30, 2008 was \$150 million compared to \$124 million for the same period in 2007. For the six month period ended June 30, 2008 and 2007, accretion expense was \$283 million and \$250 million, respectively. The increase during the periods was due to the higher

nuclear fixed asset removal and nuclear waste management liability primarily as a result of the increase in the present value of the liability due to the passage of time. In addition, during the three months ended June 30, 2008, OPG discontinued the deferral of accretion expense associated with the increase in OPG's liabilities for nuclear used fuel management and nuclear decommissioning arising from the 2006 Approved Reference Plan.

#### *Earnings on the Nuclear Fixed Asset Removal and Nuclear Waste Management Funds*

Earnings on the Nuclear Funds for the three months ended June 30, 2008 were \$108 million compared to \$209 million for the same period in 2007. For the six month period ended June 30, 2008 and 2007, earnings on the Nuclear Funds were \$57 million and \$300 million, respectively. The decrease in earnings was primarily due to lower returns on the Decommissioning Fund as a result of significant volatility and unfavourable returns in the capital markets during the second quarter of 2008 and for the first six months of 2008 compared to the same periods in 2007. In addition, during the second quarter of 2007, the earnings on the Nuclear Funds were favourably impacted due to a \$46 million reimbursement for expenditures related to the safe storage of Pickering A Units 2 and 3.

The assets in the Decommissioning Fund are invested primarily in publicly traded fixed income and equity investments. As a result, the value of these investments is subject to volatility in the capital markets. The volatility of the returns on these investments has increased, which has resulted in a negative impact on the fair value and the funded status of the Decommissioning Fund. The Decommissioning Fund has been designed to meet long-term liability requirements with a long-term strategic asset mix, and therefore, short-term market fluctuations are inevitable.

OPG's earnings from the Used Fuel Fund are not subject to the volatility of the capital markets, since the Province guarantees the rate of return on the Used Fuel Fund for the first 2.23 million used fuel bundles at 3.25 per cent per annum plus the change in the Ontario Consumer Price Index. As of June 2008, there are approximately 1.9 million used fuel bundles. The current projection indicates that the 2.23 million used fuel bundle threshold will be reached in 2012.

#### **Regulated – Hydroelectric Segment**

<i>(millions of dollars)</i>	<b>Three Months Ended June 30</b>		<b>Six Months Ended June 30</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
Regulated generation sales <sup>1</sup>	177	165	341	332
Variance accounts	-	1	1	(1)
Other	14	13	27	24
Revenue	191	179	369	355
Fuel expense	67	67	116	119
Gross margin	124	112	253	236
Operations, maintenance and administration	24	51	48	74
Depreciation and amortization	16	18	32	34
Property and capital taxes	3	2	6	7
Income before interest and income taxes	81	41	167	121

<sup>1</sup> Regulated generation sales included revenue of \$55 million and \$43 million that OPG received at the Ontario electricity spot market price for generation over 1,900 MWh in any hour during the three months ended June 30, 2008 and 2007, respectively. Regulated generation sales included revenue of \$96 million and \$90 million that OPG received at the Ontario electricity spot market price for generation over 1,900 MWh in any hour during the six months ended June 30, 2008 and 2007, respectively.

#### *Revenue*

Regulated – Hydroelectric revenue was \$191 million for the three months ended June 30, 2008 compared to \$179 million during the same period in 2007. During the six months ended June 30, 2008, Regulated – Hydroelectric revenue was \$369 million compared to \$355 million during the same period in 2007. The

increase in revenue of \$12 million and \$14 million for the three months and six months ended June 30, 2008, respectively, compared to the same periods in 2007, was primarily due to an increase in generation volume and higher prices for electricity sales over 1,900 MWh in any hour.

### Electricity Prices

During the three months ended June 30, 2008 and 2007, the average electricity sales price for the Regulated – Hydroelectric segment was 3.6¢/kWh and 3.5¢/kWh, respectively. The average electricity sales price for the six months ended June 30, 2008 and 2007 was 3.6¢/kWh. The average sales price is based on the fixed price of 3.3¢/kWh for generation up to 1,900 MWh in any hour, and the spot electricity market price for generation above this level.

### Volume

Electricity sales volume for the second quarter of 2008 was 4.9 TWh compared to 4.7 TWh during the same period in 2007. For the six months ended June 30, 2008, electricity sales volume was 9.5 TWh compared to 9.3 TWh for the same period in 2007. The increase in electricity sales volume in 2008 was primarily due to higher water flows during the periods.

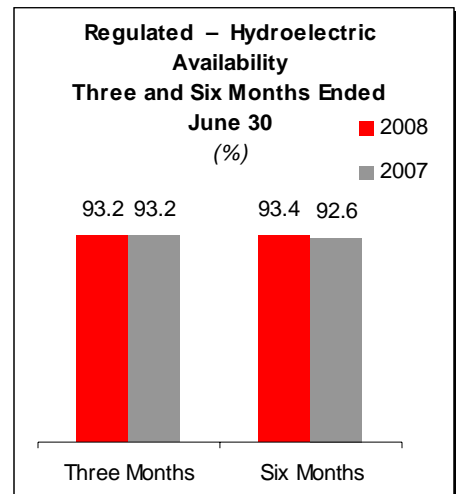
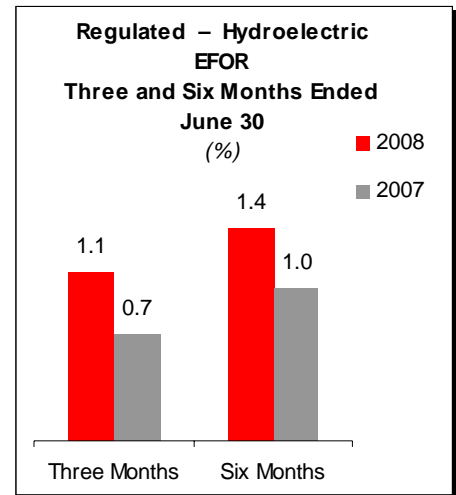
Volume related to production levels above 1,900 MWh in any hour was 1.1 TWh during the second quarter of 2008 compared to 1.0 TWh for the same period in 2007. During the six months ended June 30, 2008 and 2007, electricity generation related to production levels above 1,900 MWh in any hour was 1.9 TWh and 1.8 TWh, respectively.

The EFOR for the Regulated – Hydroelectric stations during the three months ended June 30, 2008 was 1.1 per cent compared to 0.7 per cent during the same period in 2007. During the six months ended June 30, 2008 and 2007, the EFOR for the Regulated – Hydroelectric stations was 1.4 per cent and 1.0 per cent, respectively.

The availability for the Regulated – Hydroelectric stations was 93.2 per cent for the three month periods ended June 30, 2008 and 2007. During the six months ended June 30, 2008, availability for the Regulated – Hydroelectric stations was 93.4 per cent compared to 92.6 per cent in the same period in 2007. The high availability and low EFOR reflected the continuing strong performance of the hydroelectric generating stations.

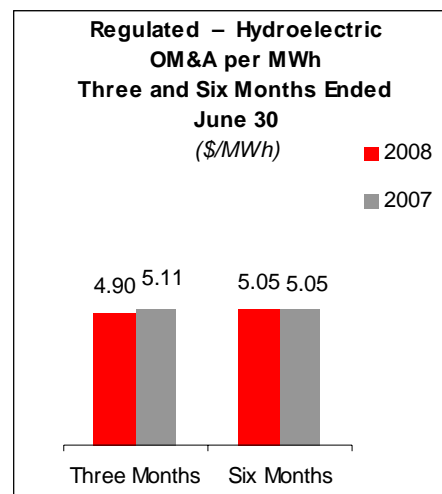
### Operations, Maintenance and Administration

OM&A expenses for the second quarter of 2008 were \$24 million compared to \$51 million for the same period in 2007. For the six months ended June 30, 2008, OM&A expenses were \$48 million compared to \$74 million during the same period in 2007. The decrease in the OM&A expense for the three and six months ended June 30, 2008 compared to the same periods in 2007 was primarily due to additional expenses in 2007 related to past grievances by First Nations.





OM&A expense per MWh for the regulated hydroelectric stations was \$4.90/MWh during the three months ended June 30, 2008 compared to \$5.11/MWh during the same period in 2007. The decrease in OM&A expense per MWh for the three months ended June 30, 2008 compared to the same period in 2007 was primarily due to higher generation. For the six month periods ended June 30, 2008 and 2007, OM&A expense per MWh for the regulated hydroelectric stations was \$5.05/MWh. OM&A expense per MWh excludes expenses related to past grievances by First Nations.



### Unregulated – Hydroelectric Segment

<i>(millions of dollars)</i>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Spot market sales, net of hedging instruments	262	184	501	399
Revenue limit rebate	(3)	(1)	(27)	(32)
Other	20	13	25	20
Revenue net of revenue limit rebate	279	196	499	387
Fuel expense	30	20	53	39
Gross margin	249	176	446	348
Operations, maintenance and administration	47	60	92	102
Depreciation and amortization	16	17	36	35
Property and capital taxes	4	1	4	5
Income before interest and income taxes	182	98	314	206

#### Revenue

Unregulated – Hydroelectric revenue was \$279 million for the three months ended June 30, 2008 compared to \$196 million for the same period in 2007. Unregulated – Hydroelectric revenue was \$499 million for the six months ended June 30, 2008 compared to \$387 million during the same period in 2007. The increase in revenue during the three and six months ended June 30, 2008 compared to the same periods in 2007 was primarily due to higher generation volume.

#### Electricity Prices

After taking into account the revenue limit rebate, OPG's average sales price for its unregulated hydroelectric generation for the three months ended June 30, 2008 and 2007 was 4.7¢/kWh and 4.6¢/kWh, respectively. OPG's average sales price for its unregulated hydroelectric generation for the six months ended June 30, 2008 and 2007 was 4.7¢/kWh.

#### Volume

During the three months ended June 30, 2008, electricity sales volume was 5.4 TWh compared to 3.9 TWh for the three months ended June 30, 2007. Electricity sales volume for the six months ended June 30, 2008 was 9.9 TWh compared to 7.8 TWh during the same period in 2007. The increase in volume during the periods was primarily due to higher water flows across the province of Ontario.

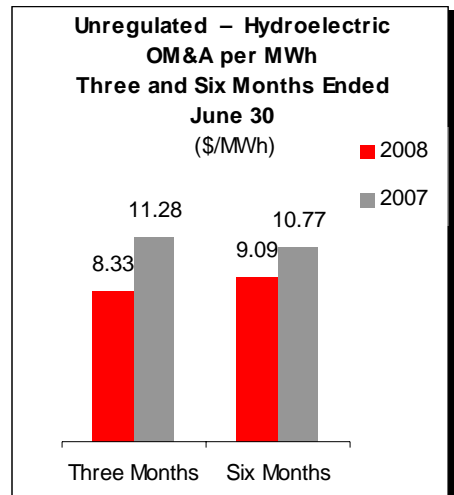
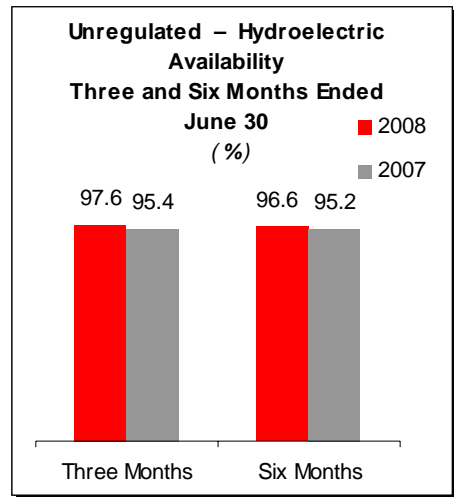
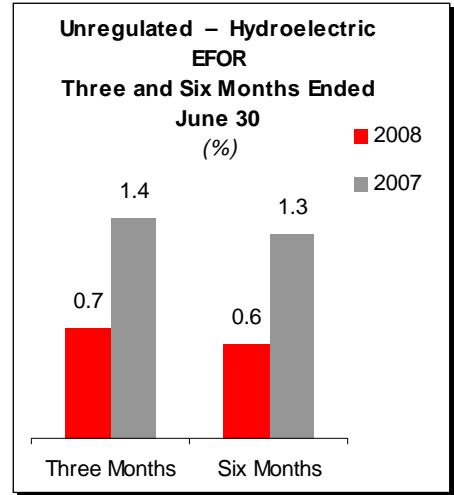
The EFOR for the Unregulated – Hydroelectric stations was 0.7 per cent in the second quarter of 2008 compared to 1.4 per cent during the same quarter in 2007. For the six months ended June 30, 2008, EFOR was 0.6 per cent compared to 1.3 per cent for the six months ended June 30, 2007.

The availability for the Unregulated – Hydroelectric stations was 97.6 per cent for the three month period ended June 30, 2008 compared to 95.4 per cent for the same period in 2007. The availability for the Unregulated – Hydroelectric stations was 96.6 per cent for the six months ended June 30, 2008 compared to 95.2 per cent for the six months ended June 30, 2007. The low EFOR and high availability reflected the continuing strong performance of the unregulated hydroelectric generating stations.

*Operations, Maintenance and Administration*

OM&A expenses for the three months ended June 30, 2008 were \$47 million compared to \$60 million for the same period in 2007. During the six months ended June 30, 2008, OM&A expenses were \$92 million compared to \$102 million for the same period last year. The decrease in OM&A expenses for the three and six months ended June 30, 2008 compared to the same periods in 2007 was primarily due to additional expenses in 2007 related to past grievances by First Nations.

OM&A expense per MWh for the unregulated hydroelectric stations was \$8.33/MWh in the second quarter of 2008 compared to \$11.28/MWh for the same quarter in 2007. During the six months ended June 30, 2008, OM&A expense per MWh for the unregulated hydroelectric stations was \$9.09/MWh compared to \$10.77/MWh for the same period in 2007. The lower OM&A expense per MWh for the three and six month periods ended June 30, 2008 was primarily due to higher generation. OM&A expense per MWh excludes expense related to past grievances by First Nations.



## Unregulated – Fossil-Fuelled Segment

<i>(millions of dollars)</i>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Spot market sales, net of hedging instruments	327	324	714	787
Revenue limit rebate	(52)	(19)	(95)	(84)
Other	32	21	66	71
Revenue, net of revenue limit rebate	307	326	685	774
Fuel expense	144	178	335	403
Gross margin	163	148	350	371
Operations, maintenance and administration	135	154	256	284
Depreciation and amortization	24	21	46	39
Accretion on fixed asset removal	2	2	4	4
Property and capital taxes	4	5	11	11
Other (gains) and losses	-	-	(2)	-
Loss (income) before interest and income taxes	(2)	(34)	35	33

### Revenue

Unregulated – Fossil-Fuelled revenue was \$307 million for the three months ended June 30, 2008 compared to \$326 million for the same period in 2007, a decrease of \$19 million. The lower revenue was primarily a result of a decrease in electricity generation of 0.8 TWh, partly offset by higher electricity prices during the three months ended June 30, 2008 compared to the same period in 2007.

Unregulated – Fossil-Fuelled revenue was \$685 million for the six months ended June 30, 2008 compared to \$774 million for the same period in 2007. The decrease in revenue of \$89 million during the first half of 2008 compared to the same period in 2007 was primarily due to lower electricity generation volume of 1.9 TWh, partly offset by higher electricity prices.

### Electricity Prices

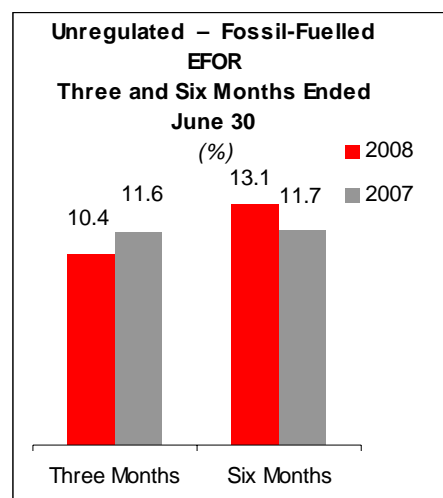
OPG's average sales price net of the revenue limit rebate for its unregulated fossil-fuelled generation was 5.0¢/kWh for the three months ended June 30, 2008 compared to 4.7¢/kWh for the three months ended June 30, 2007. During the six months ended June 30, 2008 and 2007, OPG's average sales price net of the revenue limit rebate for its unregulated fossil-fuelled generation was 4.9¢/kWh and 4.8¢/kWh, respectively.

### Volume

Electricity sales volume for the three months ended June 30, 2008 was 5.5 TWh compared to 6.3 TWh during the same period in 2007. The decrease of 0.8 TWh was primarily due to higher generation from the hydroelectric generating stations.

Electricity sales volume for the six months ended June 30, 2008 was 12.5 TWh compared to 14.4 TWh during the same period in 2007. The decrease of 1.9 TWh in 2008 was primarily due to higher generation from OPG's unregulated hydroelectric facilities and nuclear generating stations when compared to 2007.

The EFOR for the Unregulated – Fossil-Fuelled stations during the three months ended June 30, 2008 was 10.4 per cent compared to 11.6 per cent during the same period in 2007. During the six months ended June 30, 2008 and 2007, the EFOR for the Unregulated – Fossil-Fuelled stations was 13.1 per cent



and 11.7 per cent, respectively. The increase in EFOR during the six months ended June 30, 2008 was primarily due to boiler tube leaks and extensions to planned outages at the Nanticoke and Lambton generating stations during the first quarter of 2008.

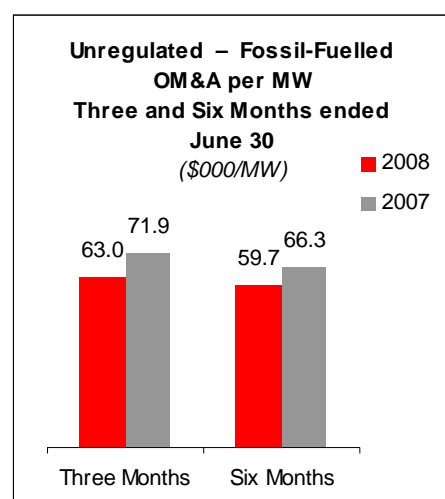
#### Fuel Expense

Fuel expense was \$144 million for the three months ended June 30, 2008 compared to \$178 million for the same period in 2007. The decrease of \$34 million was primarily due to lower electricity generation and a favourable inventory adjustment resulting from the annual fuel survey.

During the six months ended June 30, 2008, fuel expense was \$335 million compared to \$403 million during the six months ended June 30, 2007. The decrease of \$68 million in 2008 compared to 2007 was primarily due to lower electricity generation and a favourable inventory adjustment resulting from the annual fuel survey. The decrease was partly offset by higher coal contract prices and rail transportation costs, combined with higher market costs for ignition fuels.

#### Operations, Maintenance and Administration

OM&A expenses for the three months ended June 30, 2008 were \$135 million compared to \$154 million for the same period in 2007. OM&A expenses for the six months ended June 30, 2008 were \$256 million compared to \$284 million during the six months ended June 30, 2007. The decrease in OM&A expense for the three and six month periods ended June 30, 2008 compared to the same period last year was primarily due to the completion of non-recurring project work, and the impact of lower generation.



Annualized OM&A expense per MW (\$/MW) for the unregulated fossil-fueled stations decreased to \$63,000/MW for the three months ended June 30, 2008 compared to \$71,900/MW for the three months ended June 30, 2007. During the six months ended June 30, 2008, annualized OM&A expense per MW was \$59,700/MW compared to \$66,300/MW for the same period in 2007. The decrease was primarily due to lower OM&A expenses during the three and six month periods in 2008 compared to the same periods in 2007.

#### Other

(millions of dollars)	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Revenue	15	40	37	67
Operations, maintenance and administration	2	1	3	1
Depreciation and amortization	9	13	20	27
Property and capital taxes	3	3	6	6
Other (gains) and losses	-	-	9	-
Income before interest and income taxes	1	23	(1)	33

Other revenue was \$15 million for the three months ended June 30, 2008 compared to \$40 million for the same period in 2007. Other revenue for the six months ended June 30, 2008 was \$37 million compared to \$67 million in the same period in 2007. The decrease was primarily due to lower net trading revenue as a result of unrealized mark-to-market losses and lower investment income from OPG's equity investments for the three and six month periods ended June 30, 2008 compared to the same periods in 2007.

OM&A expenses of the generation business segments include an inter-segment service fee for the use of certain property, plant and equipment held within the Other category. The total service fee is recorded as a reduction to the Other category's OM&A expenses. For the three months ended June 30, 2008, the service fee was \$7 million for Regulated – Nuclear and \$3 million for Unregulated – Fossil-Fuelled, with a corresponding reduction in OM&A expenses of \$10 million for the Other category. For the three months ended June 30, 2007, the service fee was \$6 million for Regulated – Nuclear, \$1 million for Regulated – Hydroelectric, \$1 million for Unregulated – Hydroelectric, \$2 million for Unregulated – Fossil-Fuelled, with a corresponding reduction in OM&A expenses of \$10 million for the Other category.

For the six months ended June 30, 2008, the service fee was \$14 million for Regulated – Nuclear, \$1 million for Regulated – Hydroelectric, \$2 million for Unregulated – Hydroelectric, \$4 million for Unregulated – Fossil-Fuelled, with a corresponding reduction in OM&A expenses of \$21 million for the Other category. For the six months ended June 30, 2007, the service fee was \$14 million for Regulated – Nuclear, \$1 million for Regulated – Hydroelectric, \$2 million for Unregulated – Hydroelectric, \$4 million for Unregulated – Fossil-Fuelled, with a corresponding reduction in OM&A expenses of \$21 million for the Other category.

Interconnected purchases and sales, including those to be physically settled, and unrealized mark-to-market gains and losses on energy trading contracts are disclosed on a net basis in the consolidated statements of income. If disclosed on a gross basis, revenue and power purchases for the three months ended June 30, 2008 would have increased by \$52 million (three months ended June 30, 2007 – \$20 million). For the six months ended June 30, 2008, if disclosed on a gross basis, revenue and power purchases would have increased by \$103 million (six months ended June 30, 2007 – \$64 million).

The changes in the fair value of derivative instruments not qualifying for hedge accounting are recorded in Other revenue, and are carried on the consolidated balance sheets as assets or liabilities at fair value. The carrying amounts and notional quantities of the derivative instruments are disclosed in Note 12 in the unaudited interim consolidated financial statements as at and for the three and six months ended June 30, 2008.

### **Net Interest Expense**

The net interest expense for the three months ended June 30, 2008 and 2007 was \$39 million. The net interest expense for the six months ended June 30, 2008 and 2007 was \$79 million and \$65 million, respectively. The increase in net interest expense for the six months ended June 30, 2008 was primarily due to the deferral of additional interest in 2007 related to the Pickering A return to service deferral account. Interest was deferred in accordance with the requirements of the amended regulation pursuant to the *Electricity Restructuring Act, 2004* (Ontario).

### **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. Following the introduction of rate regulation on April 1, 2005, OPG has accounted 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 or refunded through future regulated prices charged to customers. As a result, OPG did not record a future tax expense of \$13 million and \$24 million for the rate regulated segments during the three months ended June 30, 2008 and 2007, respectively, which would have been recorded had OPG accounted for income taxes for the regulated segments using the liability method. During the six months ended June 30, 2008 and 2007, OPG did not record a future tax expense of \$115 million and \$42 million for the regulated segments, respectively.

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 related 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 the first quarter of 2008, a number of outstanding tax matters related to the 1999 tax audit were substantially resolved and as a result, OPG reduced its income tax liability by \$85 million. During the second quarter of 2008, all remaining issues relating to the 1999 tax audit were resolved resulting in a further reduction of OPG's income tax liability by \$21 million.

For the three months ended June 30, 2008, there was a net income tax recovery of \$8 million compared to an income tax expense of \$29 million for the same period in the prior year. For the six months ended June 30, 2008, there was a net income tax recovery of \$16 million compared to an income tax expense of \$86 million for the same period in the prior year. The decrease in the income tax expense was due to the reduction in 2008 of the income tax liability to reflect the resolution of tax uncertainties related to OPG's 1999 taxation year.

The audit of OPG's taxation years subsequent to 1999 is expected to commence in late 2008. Should the outcome of the audit for subsequent years differ from OPG's recorded income tax liabilities, the Company's effective tax rate and its net income could be materially affected either negatively or positively in the period in which the matters are resolved.

## LIQUIDITY AND CAPITAL RESOURCES

OPG's primary sources of liquidity and capital are funds generated from operations, bank financing and credit facilities provided by the OEFC. These sources are utilized for continued investment in plant and technologies, and to meet other significant funding obligations including contributions to the Pension Fund, the Used Fuel and Decommissioning Funds, and to service and repay long-term debt and revenue limit rebate obligations.

<i>(millions of dollars)</i>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Cash and cash equivalents, beginning of the period	303	15	110	6
Cash flow provided by operating activities	152	312	401	475
Cash flow used in investing activities	(139)	(171)	(267)	(335)
Cash flow provided by (used in) financing activities	49	(18)	121	(8)
Net increase	62	123	255	132
Cash and cash equivalents, end of the period	365	138	365	138

### Operating Activities

Cash flow provided by operating activities for the three months ended June 30, 2008 was \$152 million compared to cash flow provided by operating activities of \$312 million for the same period in 2007. The decrease in cash flow was primarily due to a lower reimbursement of expenditures for nuclear fixed asset removal and nuclear waste management during the second quarter of 2008 compared to the same quarter in 2007, and a decrease in cash receipts from non-energy revenue.

Cash flow provided by operating activities for the six months ended June 30, 2008 was \$401 million compared to cash flow provided by operating activities of \$475 million for the same period in 2007. The decrease in cash flow was primarily due to an increase in nuclear fuel expenditures, a lower reimbursement of expenditures for nuclear fixed asset removal and nuclear waste management, and higher revenue limit rebate payments. The decrease in cash flow was partially offset by higher cash receipts from generation activities and lower tax instalment payments.

## **Investing Activities**

OPG is in a capital-intensive business that requires continued investment in plant and technologies to improve operating efficiencies, increase generating capacity of its existing stations, invest in new generating stations and to maintain and improve service, reliability, safety and environmental performance.

Investment in fixed assets during the three months ended June 30, 2008 was \$134 million compared with \$163 million for the second quarter of 2007. For the six months ended June 30, 2008, investment in fixed assets was \$262 million compared with \$297 million for the six months ended June 30, 2007. The decrease was primarily due to lower capital expenditures for the Portlands Energy Centre. OPG's forecast capital expenditures for 2008 are approximately \$780 million, which include amounts for the Niagara Tunnel, Portlands Energy Centre and other nuclear and hydroelectric development projects.

For the six months ended June 30, 2008, investing activities included costs deferred as regulatory assets of \$10 million compared to \$38 million during the same period in 2007. The amounts deferred as regulatory assets included interest expense related to the Pickering A return to service deferral account, and non-capital costs incurred for nuclear generation development initiatives.

## **Financing Activities**

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 has 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 June 30, 2008, no commercial paper was outstanding (December 31, 2007 – nil), 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 and Hound Chute project. As at June 30, 2008, there was no borrowing under this credit facility. OPG is also pursuing external project financing for up to \$200 million for this project.

OPG also maintains \$25 million (December 31, 2007 – \$25 million) in short-term uncommitted overdraft facilities and \$238 million (December 31, 2007 – \$238 million) of short-term uncommitted credit facilities, which support the issuance of Letters of Credit. OPG uses Letters of Credit to support its supplementary pension plans and for other purposes. At June 30, 2008, there was a total of \$205 million of Letters of Credit issued (December 31, 2007 – \$205 million), which included \$175 million for the supplementary pension plans (December 31, 2007 – \$175 million) and \$16 million related to the construction and operation of the Portlands Energy Centre (December 31, 2007 – \$16 million).

OPG has an agreement with the OEFC to finance the Niagara Tunnel project for up to \$1 billion over the duration of the project. The funding is advanced in the form of 10-year notes, on commercial terms and conditions. Advances under this facility commenced in October 2006, and amounted to \$310 million as at June 30, 2008, including \$30 million of new borrowing during the second quarter of 2008. Similarly, debt financing has been negotiated with the OEFC for OPG's interest in the Portlands Energy Centre and the Lac Seul project for up to \$400 million and \$50 million, respectively. Advances under these facilities commenced in December 2006, and totalled \$265 million for the Portlands Energy Centre and \$20 million for the Lac Seul project as at June 30, 2008. This included \$20 million of new borrowing under the Portlands Energy Centre facility in the second quarter of 2008.

As at June 30, 2008, OPG's long-term debt outstanding with the OEFC was \$3.8 billion. Although the new borrowings added in 2008 has extended the maturity profile, approximately \$2.3 billion of long-term debt must be repaid or refinanced within the next five years. To ensure that adequate financing resources are available beyond its \$1 billion commercial paper program backed by the bank credit facility, OPG reached an agreement with the OEFC in 2007 for a \$950 million credit agreement to refinance senior notes as they mature over the period from September 2007 to September 2009.

## BALANCE SHEET HIGHLIGHTS

The following section provides highlights of OPG's unaudited interim consolidated financial position using selected balance sheet data:

Selected balance sheet data <i>(millions of dollars)</i>	As at	
	June 30 2008	December 31 2007
Assets		
Accounts receivable	366	315
Property, plant and equipment – net	12,739	12,777
Nuclear fixed asset removal and nuclear waste management funds	9,539	9,263
Regulatory assets	369	356
Future income taxes	57	-
Liabilities		
Accounts payable and accrued charges	831	953
Long-term debt (including debt due within one year)	3,974	3,853
Fixed asset removal and nuclear waste management	11,187	10,957
Long-term accounts payable and accrued charges	440	184
Future income taxes	-	217

### Accounts Receivable

As at June 30, 2008, accounts receivable were \$366 million compared to \$315 million as at December 31, 2007. The increase of \$51 million was primarily due to higher electricity generation volumes in June 2008 compared to December 2007.

### Property, Plant and Equipment – Net

Net property, plant and equipment as at June 30, 2008 was \$12,739 million compared to \$12,777 million as at December 31, 2007. The decrease of \$38 million was primarily due to depreciation expense, partially offset by additions to fixed assets.

### Nuclear Fixed Asset Removal and Nuclear Waste Management Funds

#### *Decommissioning Fund*

The Decommissioning Fund was established to fund the future costs of nuclear fixed asset removal and long-term low and intermediate level nuclear waste management and a portion of used fuel storage costs after station life. Upon termination of the Ontario Nuclear Funds Agreement ("ONFA"), the Province has a right to any excess funding in the Decommissioning Fund, which is the excess of the fair market value of the Decommissioning Fund assets over the estimated completion costs as per the most recently approved ONFA Reference Plan. When the Decommissioning Fund is overfunded, OPG limits the earnings it recognizes in its consolidated financial statements, through a charge to the Decommissioning Fund with a corresponding payable to the Province, such that the balance of the Decommissioning Fund would equal the cost estimate of the liability based on the most recently approved ONFA reference plan. The payable to the Province could be reduced in subsequent periods in the event that the Decommissioning Fund earns less than its target rate of return or in the event that a new ONFA reference plan is approved with a higher estimated decommissioning liability. When the Decommissioning Fund is underfunded, the earnings for the Decommissioning Fund reflect actual fund returns based on the market value of the assets.

The Decommissioning Fund's asset value on a fair value basis was \$4,993 million at June 30, 2008 compared to \$5,072 million as at December 31, 2007. The decrease in asset value in the



Decommissioning Fund of \$79 million was primarily due to unfavourable returns in the capital markets during the first half of 2008. As at December 31, 2007, the Decommissioning Fund was overfunded by \$3 million when compared to the 2006 ONFA reference plan cost to complete, and the fund balance was reduced by a payable to the Province. The Decommissioning Fund was underfunded at June 30, 2008, and as a result the payable to the Province was nil.

#### *Used Fuel Fund*

Under the ONFA, the Province guarantees OPG's annual return in the Used Fuel Fund at 3.25 per cent plus the change in the Ontario Consumer Price Index ("committed return") for funding related to the first 2.23 million used fuel bundles. OPG recognizes the committed return on the Used Fuel Fund and includes it in the earnings on the nuclear fixed asset removal and nuclear waste management funds. The difference between the committed return on the Used Fuel Fund and the actual market return, based on the fair value of the Used Fuel Fund's assets, which includes realized and unrealized returns, is recorded as due to or due from the Province. The asset values as at June 30, 2008 and December 31, 2007, were offset by a payable to the Province of \$339 million and \$511 million, respectively. The offset relates to the committed return adjustment. At June 30, 2008, the Used Fuel Fund asset value on a fair value basis was \$4,546 million compared to \$4,191 million as at December 31, 2007. The increase in the value of the Used Fuel Fund assets was due to the committed return and new contributions to the fund.

The market volatility during the first half of 2008 did not have a significant impact on the Used Fuel Fund balance as a result of the Province's rate of return guarantee.

#### **Regulatory Assets**

As at June 30, 2008, regulatory assets were \$369 million compared to \$356 million as at December 31, 2007. The increase in regulatory assets was primarily due to an increase in the deferral account during the first quarter of 2008, related to the increase in OPG's liabilities for nuclear used fuel management and nuclear decommissioning and low and intermediate level waste management arising from the 2006 Approved Reference Plan, and the application of interest. This increase was partially offset by the amortization of the Pickering A Return to Service deferral account.

Commencing in the second quarter of 2008, OPG ceased recording any additions to variance and deferral accounts, pending the outcome of the OEB's decision regarding the re-establishment of these accounts. With the exception of the Pickering A Return to Service deferral account, OPG will not amortize any other regulatory assets or liabilities until it receives new payment amounts that include recovery of regulatory assets and settlement of regulatory liabilities. OPG continued to amortize the Pickering A Return to Service deferral account in the second quarter as the balance in this account is being recovered through existing regulated rates. In addition, OPG continued to record interest on the regulatory assets and liabilities in the second quarter and will continue to do so until the balances in these accounts are recovered.

#### **Accounts Payable and Accrued Charges**

Accounts payable and accrued charges as at June 30, 2008 were \$831 million compared to \$953 million as at December 31, 2007. The decrease of \$122 million was primarily due to reduced trade accounts payable and accrued charges, including lower payables related to uranium purchases and outage related expenditures, partially offset by an increase in the liability for short-term mark-to-market losses.

#### **Long-Term Debt (including debt due within one year)**

Long-term debt as at June 30, 2008 was \$3,974 million compared to \$3,853 million as at December 31, 2007. The increase was primarily due to the issuance of long-term debt of \$200 million under the \$950 million credit agreement to refinance maturing notes, \$70 million under the Niagara Tunnel facility, and \$55 million under the Portlands Energy Centre facility. The increase was partially offset by repayment of long-term debt of \$204 million.

## **Fixed Asset Removal and Nuclear Waste Management**

The liability for fixed asset removal (for nuclear and fossil-fuelled generating stations) and nuclear waste management as at June 30, 2008 was \$11,187 million compared to \$10,957 million as at December 31, 2007. The increase was primarily due to accretion due to the passage of time, partially offset by expenditures on nuclear waste management activities.

## **Long-term Accounts Payable and Accrued Charges and Future Income Tax Asset and Liability**

As at June 30, 2008, long-term accounts payable and accrued charges included various contingent liabilities and unrealized mark-to-market losses. The resolution of tax uncertainties related to the 1999 taxation year also impacted the future income tax liability as at June 30, 2008.

## **Accumulated Other Comprehensive (Loss) Income**

Accumulated other comprehensive loss as at June 30, 2008 was \$17 million and accumulated other comprehensive income as at December 31, 2007 was \$17 million. Accumulated other comprehensive (loss) income reflects the balances related to derivative instruments and amounts that are designated for hedging purposes net of income taxes.

## **Off-Balance Sheet Arrangements**

In the normal course of operations, OPG engages in a variety of transactions that, under Canadian GAAP, are either not recorded in the Company's consolidated financial statements or are recorded in the Company's consolidated financial statements in amounts that differ from the full contract amounts. Principal off-balance sheet activities that OPG undertakes include securitization of certain accounts receivable agreements, guarantees, which provide financial or performance assurance to third parties on behalf of certain subsidiaries, and long-term fixed price contracts.

## **CHANGES IN ACCOUNTING POLICIES**

### *Capital Disclosures and Financial Instruments*

In December 2006, the CICA issued three new accounting standards: Handbook Section 1535, *Capital Disclosures* ("Section 1535"), Handbook Section 3862, *Financial Instruments – Disclosures* ("Section 3862"), and Handbook Section 3863, *Financial Instruments – Presentation* ("Section 3863"). These new standards are effective for the Company beginning January 1, 2008.

Section 1535 specifies the disclosure of (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such non-compliance.

Sections 3862 and 3863 replace Handbook Section 3861, *Financial Instruments – Disclosure and Presentation*, revising and enhancing the disclosure requirements, and carrying forward unchanged the presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks.

### *Inventories*

The CICA issued a new accounting standard, Section 3031, *Inventories*, in March 2007, which is based on International Accounting Standard ("IAS") 2. The new section replaced the existing Section 3030, *Inventories*. Under the new 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". The new 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 new accounting standard and the consequential amendments

are 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.

#### *Accounting for Regulatory Operations*

In December 2007, the CICA revised its guidance on accounting for rate-regulated operations. The revision resulted in amendments to Handbook Sections 1100, *Generally Accepted Accounting Principles*, and 3465, *Income Taxes*, and Accounting Guideline 19 (“AcG-19”), *Disclosures by Entities Subject to Rate Regulation*, as follows:

- to remove the temporary exemption pertaining to the application of Section 1100 to rate-regulated operations, including the elimination of the opportunity to use industry practice as an acceptable basis for recognition and measurement of assets and liabilities arising from rate regulation;
- to amend Section 3465 to require the recognition of future income tax liabilities and assets as well as a separate regulatory asset or liability for the amount of future income taxes expected to be included in future rates and recovered from or paid to customers; and
- to amend AcG-19, as necessary, as a result of amendments to Sections 1100 and 3465.

As a result of the changes to Section 3465, OPG will be required to recognize future income taxes associated with its rate-regulated operations in the same manner as it currently recognizes future income taxes for its unregulated operations. OPG will apply the changes prospectively to interim and annual financial consolidated statements beginning January 1, 2009. OPG is currently evaluating the impact of implementing these changes on its consolidated financial statements.

#### *Conversion to International Financial Reporting Standards*

In February 2008, the Canadian Accounting Standards Board confirmed that Publicly Accountable Enterprises will be required to transition from Canadian GAAP to International Financial Reporting Standards (“IFRS”) for interim and annual financial reporting purposes for fiscal years beginning on or after January 1, 2011. OPG is required to present its first set of published IFRS statements in the first quarter of 2011, with comparative information. In May 2008, the Canadian Securities Administrators issued Staff Notice 52-320, which provides guidance on the disclosure of changes in expected accounting policies related to the change over to IFRS. In accordance with the notice, OPG is required to provide an update of the Company’s IFRS conversion plan in each financial reporting period prior to conversion on January 1, 2011.

OPG commenced its IFRS conversion project in 2007 and has established a formal project governance structure. This structure includes a steering committee consisting of senior levels of management from finance, representatives from all business units, and information technology. There is regular reporting to executive management and to the Audit/Risk Committee of the Board of Directors. OPG has also engaged an external expert advisor.

OPG’s conversion project consists of three phases: diagnostic, development, and implementation. During the fourth quarter of 2007, OPG completed the diagnostic phase which involved a high level review of the major differences between current Canadian GAAP and IFRS. Currently, OPG has determined that the differences with the highest potential to impact OPG’s accounting include rate regulated accounting, accounting for fixed assets, asset retirement obligation accounting, as well as initial adoption of IFRS under the provision of IFRS 1, *First-time Adoption of IFRS*.

During 2008, OPG has completed a number of milestones as part of the development stage of its IFRS conversion project, which requires a more detailed consideration of those issues identified by the diagnostic exercise as well as a more thorough review of all of the accounting differences, and related system and process impacts. These milestones include the completion of technical training for each of the components that OPG has identified as significant and the completion of a number of component evaluations. OPG has established a communication plan and has met each of the deliverables to date. OPG has begun the process of developing comprehensive staff training programs.

## RISK MANAGEMENT

A detailed discussion of OPG's governance structure and inherent risks is included in the 2007 annual MD&A under the heading, *Risk Management*. The following discussion updates the annual disclosure.

### Market and Credit Risks

#### *Commodities*

Changes in the market price of electricity or of the fuels used to produce electricity can adversely impact OPG's earnings and cash flow from operations. To manage this risk, the Company seeks to maintain a balance between the commodity price risk inherent in its electricity production and plant fuel portfolios to the extent that trading liquidity in the relevant commodities markets provides the economic opportunity to do so. To manage fuel price risk, OPG has a fuel hedging program, which includes using fixed price and indexed contracts, as well as approved derivative products. During the past quarter unexpected interruptions in global supply have caused coal prices to escalate significantly. The impact of the escalation has not, however, impacted fuel costs significantly due to the long-term nature of the hedge program.

The rise in prices has increased the Company's potential credit exposure to coal suppliers from \$62 million at the end of 2007 to \$615 million at June 30, 2008, given the increase in value of the existing contracts. Potential credit exposure is OPG's assessment of maximum exposure over the life of each transaction at a 95 per cent confidence interval. In order to mitigate this risk, OPG maintains credit policies, including evaluation of counterparty financial condition and the use of standard contracts. As well, to diversify risk OPG sources its coal requirements from over 15 different counterparties.

The percentages of OPG's expected generation, emission requirements and fuel requirements hedged are shown below:

	2008	2009	2010
Estimated generation output hedged <sup>1</sup>	93%	74%	66%
Estimated fuel requirements hedged <sup>2</sup>	98%	97%	83%
Estimated nitric oxide ("NO") emission requirement hedged <sup>3</sup>	100%	100%	100%
Estimated SO <sub>2</sub> emission requirement hedged <sup>3</sup>	100%	100%	100%

<sup>1</sup> Represents the portion of megawatt hours of expected future generation production, including power purchases, for which the Company has sales commitments and contracts including the obligations under regulated pricing commitments, agreements with the IESO, OPA auction sales and the revenue limit on OPG's non-prescribed assets (which ends on April 30, 2009).

<sup>2</sup> Represents the approximate portion of megawatt hours of expected generation production (and fossil year-end inventory target) from all types of facilities (fossil, nuclear and hydroelectric) for which OPG has entered into some form of contractual arrangements or obligations in order to secure either the expected availability and/or price of fuel and/or fuel related services. Excess fuel in inventories in a given year is attributed to the next year for the purpose of measuring hedge ratios. Since production from hydroelectric facilities is primarily influenced by expected weather and weather patterns, fuel hedge ratios for hydroelectric facilities are assumed to be 100 per cent.

<sup>3</sup> Represents the approximate portion of megawatt hours of expected fossil production for which OPG has purchased, been allocated or granted emission allowances and Emission Reduction Credits to meet OPG's obligations under Ontario Environmental Regulation 397/01.

#### *Interest Rates*

OPG periodically uses interest rate swap agreements to mitigate elements of interest rate risk exposure associated with anticipated new financing. As of June 30, 2008, OPG had total forward start interest rate swap contracts outstanding with a notional principal of \$472 million and a maturity schedule of one to 12 years.

## Trading

Open trading positions are subject to measurement against Value at Risk (“VaR”) limits. For a given portfolio, VaR measures the possible future loss in terms of market value, which under normal market conditions will not be exceeded within a defined probability and time period. Currently, VaR limits for trading are \$5 million, and VaR utilization ranged between \$3.3 million and \$1.9 million during the three months ended June 30, 2008, compared to \$0.9 million and \$1.9 million during the three months ended March 31, 2007. VaR utilization is closely monitored in order to ensure compliance with approved limits.

## Regulatory Risks

Addressing nuclear regulatory requirements adds to the cost of operations and in some instances, may result in a reduction in the productive capacity of a nuclear generating station. This is currently the case at the Pickering A nuclear generating station, where the units are derated to 96 per cent of full capacity. OPG is expecting the derating could be extended through part of 2009.

The Company is subject to certain regulatory risk in regard to the pending approval by the OEB of new payment amounts for OPG’s regulated facilities, including the OEB’s decision on retrospective recovery of new payment amounts between April 1, 2008 and the effective date of the OEB’s final order. Specifically, the effective date of the OEB’s order and the decision on retrospective recovery may impact the amount of regulatory assets and liabilities currently on OPG’s consolidated balance sheet retroactive to April 1, 2008. In addition, the OEB’s decision could result in adjustments to the existing regulatory assets and liabilities on OPG’s consolidated balance sheet.

## CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

During the most recent interim period, there have been no changes in the Company’s policies and procedures and other processes that comprise its internal control over financial reporting, that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

## QUARTERLY FINANCIAL HIGHLIGHTS

The following tables set out selected financial information from OPG’s unaudited interim consolidated financial statements for each of the eight most recently completed quarters. This financial information has been prepared in accordance with Canadian GAAP.

<i>(millions of dollars)</i>	<b>June 30 2008</b>	March 31 2008	December 31 2007	September 30 2007
Revenue after revenue limit rebate	<b>1,385</b>	1,563	1,342	1,421
Net income	<b>99</b>	162	119	113
Net income per share	<b>\$0.39</b>	\$0.63	\$0.46	\$0.44

<i>(millions of dollars)</i>	June 30 2007	March 31 2007	December 31 2006	September 30 2006
Revenue after revenue limit rebate	1,373	1,524	1,276	1,435
Net income (loss)	125	171	(19)	167
Net income (loss) per share	\$0.49	\$0.67	\$(0.08)	\$0.65

OPG’s quarterly results are impacted by changes in demand primarily 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.

Additional items which impacted net income (loss) in certain quarters above include the following:

- Decrease in depreciation expense primarily due to extension of the service life, for accounting purposes, of all coal-fired generating stations to December 31, 2012, beginning in the third quarter of 2006;
- Impairment loss on the Thunder Bay and Atikokan coal-fired generating stations of \$22 million, reflecting the carrying value of the stations, during the fourth quarter of 2006;
- Higher OM&A expense in 2007 primarily due to higher outage and other maintenance expenditures at OPG's nuclear and fossil-fuelled generating stations, and expenses related to past grievances by First Nations;
- Decrease in gross margin from electricity sales during the first quarter of 2007 primarily due to lower generation from OPG's nuclear generating stations as a result of an unplanned outage during the first quarter of 2007 at the Pickering B nuclear generation station caused by an inadvertent release of resin by a third-party contractor from the water treatment plant into the demineralized water system, and the requirement for maintenance related to the recovery of the resin. In addition, nuclear generation was also impacted by an extension to a planned outage during the first quarter of 2007 at the Pickering A nuclear generating station for significant additional repair work required as a result of a component failure during inspection;
- Higher earnings from the Nuclear Funds during the second quarter of 2007 primarily due to a higher Ontario CPI during the second quarter of 2007, which impacted the guaranteed return on the Used Fuel Fund. In addition, the increase in earnings also reflected a reimbursement from the Nuclear Funds for expenditures related to the safe storage of Pickering A Units 2 and 3;
- Lower gross margin primarily due to lower nuclear generation during the three months ended September 30, 2007 as a result of the shutdown of the Pickering A nuclear generating station Units 1 and 4 to perform modifications on a backup electrical system;
- Higher earnings due to a recovery of \$20 million related to the re-estimation of costs to complete the remaining work to remediate the Lakeview site during the fourth quarter of 2007;
- Impairment losses of \$10 million reflecting the fair market value of OPG's third-party ABCP holdings during the fourth quarter of 2007;
- Lower income tax expense during the fourth quarter of 2007 largely due to an additional contribution of \$334 million to the Nuclear Funds. Contributions are deductible for tax purposes and no offsetting future tax expense is recognized by OPG due to the use of the taxes payable method to account for income taxes in the regulated segment;
- Decrease in income tax expense of \$85 million and \$21 million during the first and second quarters of 2008, respectively, was due to the resolution of the tax uncertainties related to the audit of OPG's 1999 taxation year; and
- Decrease in earnings due to lower returns on the Decommissioning Fund, as a result of significant volatility and unfavourable returns in the capital markets during the first and second quarters of 2008.

## SUPPLEMENTAL EARNINGS MEASURES

In addition to providing net income in accordance with Canadian GAAP, OPG's MD&A, unaudited interim consolidated financial statements as at and for the three and six months ended June 30, 2008 and 2007 and the notes thereto, present certain non-GAAP financial measures. These financial measures do not have standard definitions prescribed by Canadian GAAP and therefore may not be comparable to similar measures disclosed by other companies. OPG utilizes these measures in making operating decisions and assessing its performance. Readers of the MD&A, consolidated financial statements and notes thereto utilize these measures in assessing the Company's financial performance from ongoing operations. These non-GAAP financial measures have not been presented as an alternative to net income in accordance with Canadian GAAP as an indicator of operating performance. The definitions of the non-GAAP financial measures are as follows:

(1) **Gross margin** is defined as revenue less revenue limit rebate and fuel expense.

(2) **Earnings** are defined as net income.

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## INTERIM CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
<i>(millions of dollars except where noted)</i>				
<b>Revenue (Note 16)</b>				
Revenue before revenue limit rebate	1,440	1,393	3,070	3,013
Revenue limit rebate (Note 15)	(55)	(20)	(122)	(116)
	<b>1,385</b>	1,373	<b>2,948</b>	2,897
Fuel expense (Note 16)	277	298	581	626
<b>Gross margin (Note 16)</b>	<b>1,108</b>	1,075	<b>2,367</b>	2,271
<b>Expenses</b>				
Operations, maintenance and administration	750	776	1,441	1,470
Depreciation and amortization (Note 5)	160	169	335	351
Accretion on fixed asset removal and nuclear waste management liabilities (Note 9)	152	126	287	254
Earnings on nuclear fixed asset removal and nuclear waste management funds (Note 9)	(108)	(209)	(57)	(300)
Property and capital taxes	24	20	30	49
	<b>978</b>	<b>882</b>	<b>2,036</b>	1,824
<b>Income before the following:</b>	<b>130</b>	193	<b>331</b>	447
Other losses (Note 3 and 16)	-	-	7	-
<b>Income before interest and income taxes</b>	<b>130</b>	193	<b>324</b>	447
Net interest expense (Note 8)	39	39	79	65
<b>Income before income taxes</b>	<b>91</b>	154	<b>245</b>	382
Income tax expenses (Note 10)				
Current	(12)	29	146	77
Future	4	-	(162)	9
	<b>(8)</b>	29	<b>(16)</b>	86
<b>Net income</b>	<b>99</b>	125	<b>261</b>	296
<b>Basic and diluted income per common share (dollars)</b>	<b>0.39</b>	0.48	<b>1.02</b>	1.15
<b>Common shares outstanding (millions)</b>	<b>256.3</b>	256.3	<b>256.3</b>	256.3

See accompanying notes to the consolidated financial statements



## INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

<i>(millions of dollars)</i>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
<b>Operating activities</b>				
Net income	99	125	261	296
Adjust for non-cash items:				
Depreciation and amortization <i>(Note 5)</i>	160	169	335	351
Accretion on fixed asset removal and nuclear waste management liabilities <i>(Note 9)</i>	152	126	287	254
Earnings on nuclear fixed asset removal and nuclear waste management funds	(108)	(209)	(57)	(300)
Pension and other post employment benefit costs <i>(Note 11)</i>	106	121	212	243
Future income taxes <i>(Note 10)</i>	4	-	(162)	9
Other	30	54	49	64
	<b>443</b>	<b>386</b>	<b>925</b>	<b>917</b>
Contributions to nuclear fixed asset removal and nuclear waste management funds	(113)	(113)	(227)	(227)
Expenditures on fixed asset removal and nuclear waste management	(41)	(47)	(95)	(100)
Reimbursement of expenditures on nuclear fixed asset removal and nuclear waste management	-	74	8	86
Contributions to Pension Fund	(66)	(66)	(132)	(132)
Expenditures on other post employment benefits and supplementary pension plans	(23)	(17)	(39)	(34)
Revenue limit rebate <i>(Note 15)</i>	(30)	(26)	(96)	(48)
Expenditure on restructuring	-	-	-	(2)
Net changes to other long-term assets and liabilities	5	(15)	132	(19)
Changes in non-cash working capital balances <i>(Note 17)</i>	(23)	136	(75)	34
<b>Cash flow provided by operating activities</b>	<b>152</b>	<b>312</b>	<b>401</b>	<b>475</b>
<b>Investing activities</b>				
Increase in regulatory assets <i>(Note 6)</i>	(4)	(8)	(10)	(38)
Investment in fixed assets	(134)	(163)	(262)	(297)
Net proceeds from sale (purchase) of long-term investments	(1)	-	5	-
<b>Cash flow used in investing activities</b>	<b>(139)</b>	<b>(171)</b>	<b>(267)</b>	<b>(335)</b>
<b>Financing activities</b>				
Issuance of long-term debt <i>(Note 7)</i>	50	160	325	210
Repayment of long-term debt <i>(Note 7)</i>	(1)	(1)	(204)	(203)
Net decrease in short-term notes	-	(177)	-	(15)
<b>Cash flow provided by (used in) financing activities</b>	<b>49</b>	<b>(18)</b>	<b>121</b>	<b>(8)</b>
<b>Net increase in cash and cash equivalents</b>	<b>62</b>	<b>123</b>	<b>255</b>	<b>132</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>303</b>	<b>15</b>	<b>110</b>	<b>6</b>
<b>Cash and cash equivalents, end of period</b>	<b>365</b>	<b>138</b>	<b>365</b>	<b>138</b>

See accompanying notes to the interim consolidated financial statements

## INTERIM CONSOLIDATED BALANCE SHEETS (UNAUDITED)

<b>As at</b> <i>(millions of dollars)</i>	<b>June 30</b> <b>2008</b>	<b>December 31</b> <b>2007</b>
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	365	110
Accounts receivable <i>(Note 4)</i>	366	315
Fuel inventory	591	604
Prepaid expenses	25	35
Future income taxes <i>(Note 10)</i>	7	12
Materials and supplies <i>(Note 2)</i>	128	125
	<b>1,482</b>	<b>1,201</b>
<b>Fixed assets <i>(Note 2 and 16)</i></b>		
Property, plant and equipment	17,979	17,772
Less: accumulated depreciation	5,240	4,995
	<b>12,739</b>	<b>12,777</b>
<b>Other long-term assets</b>		
Deferred pension asset	769	731
Nuclear fixed asset removal and nuclear waste management funds <i>(Note 9)</i>	9,539	9,263
Long-term investments <i>(Note 3)</i>	85	93
Long-term materials and supplies	332	353
Future income tax asset <i>(Note 10)</i>	57	-
Regulatory assets <i>(Note 6)</i>	369	356
Long-term accounts receivable and other assets	36	65
	<b>11,187</b>	<b>10,861</b>
	<b>25,408</b>	<b>24,839</b>

See accompanying notes to the interim consolidated financial statements

## INTERIM CONSOLIDATED BALANCE SHEETS (UNAUDITED)

As at <i>(millions of dollars)</i>	June 30 2008	December 31 2007
<b>Liabilities</b>		
<b>Current liabilities</b>		
Accounts payable and accrued charges	831	953
Revenue limit rebate payable <i>(Note 15)</i>	126	100
Long-term debt due within one year <i>(Note 7)</i>	382	407
Deferred revenue due within one year	12	12
Income and capital taxes payable	41	66
	<u>1,392</u>	<u>1,538</u>
<b>Long-term debt <i>(Note 7)</i></b>	<u>3,592</u>	<u>3,446</u>
<b>Other long-term liabilities</b>		
Fixed asset removal and nuclear waste management <i>(Note 9)</i>	11,187	10,957
Other post employment benefits and supplementary pension plans	1,635	1,556
Long-term accounts payable and accrued charges	440	184
Deferred revenue	115	120
Future income taxes <i>(Note 10)</i>	-	217
Regulatory liabilities <i>(Note 6)</i>	13	14
	<u>13,390</u>	<u>13,048</u>
<b>Shareholder's equity</b>		
Common shares	5,126	5,126
Retained earnings	1,925	1,664
Accumulated other comprehensive (loss) income	(17)	17
	<u>7,034</u>	<u>6,807</u>
	<u>25,408</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)**

**Six Months Ended June 30**

*(millions of dollars)*

	<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>261</b>	296
Balance at end of period	<b>1,925</b>	1,432
<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>(34)</b>	29
Balance at end of period	<b>(17)</b>	50
<b>Total shareholder's equity at end of period</b>	<b>7,034</b>	6,608

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

*(millions of dollars)*

	<b>Three Months Ended June 30 2008</b>	<b>Six Months Ended June 30 2008</b>
<b>Net income</b>	<b>99</b>	<b>261</b>
<b>Other comprehensive (loss) income, net of income tax</b>		
Net (loss) on derivatives designated as cash flow hedges <sup>1</sup>	<b>(3)</b>	<b>(30)</b>
Reclassification to income of gains on derivatives designated as cash flow hedges <sup>2</sup>	-	<b>(4)</b>
Other comprehensive (loss) income for the period	<b>(3)</b>	<b>(34)</b>
<b>Comprehensive income</b>	<b>96</b>	<b>227</b>

<sup>1</sup> Net of income tax recoveries of \$Nil and \$3 million for the three and six months ended June 30, 2008, respectively.

<sup>2</sup> Net of income tax recoveries of \$2 million and \$3 million for the three and six months ended June 30, 2008, respectively.

*See accompanying notes to the interim consolidated financial statements*

## **NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND SIX MONTHS ENDED JUNE 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 was introduced pursuant to the *Electricity Restructuring Act, 2004* (Ontario), which provides that, effective April 1, 2005, OPG received 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 held a hearing to consider OPG's request that payment amounts for its regulated facilities be declared interim, effective April 1, 2008, and OPG's request for an interim increase in payment amounts. In its decision, the OEB did not approve an interim increase in the payment amounts, but granted OPG's request that payment amounts be made interim, effective April 1, 2008. This decision preserves the opportunity for OPG to recover the difference between final payment amounts as approved by the OEB and the current payment amounts for the period between April 1, 2008 and the date of the OEB's final order.

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 the above 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 such 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 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.

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.

### *Inventories*

The CICA issued Section 3031, Inventories, in March 2007, which is based on International Accounting Standard (“IAS”) 2. The section replaced the existing Section 3030, Inventories. Under the 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. The 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 statements of income for the three and six months ended June 30, 2008.

## **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 \$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 gains and 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. The sanctioning of the Plan by the Ontario Superior Court was delayed until June 2008, to incorporate certain amendments to the Plan. Despite the ruling of the Ontario Superior Court, a motion by a number of noteholders opposing the sanctioning of the Plan went before the Ontario Court of Appeal. In August 2008, the Ontario Court of Appeal upheld the earlier decision of the Ontario Superior Court. Absent a further appeal to the Supreme Court of Canada by noteholders who objected to the restructuring, the committee of large noteholders expects the Plan to close by September 30, 2008. OPG continues to monitor events related to the Plan and its implementation.

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>	Principal Amount of Receivables as at	
	June 30 2008	December 31 2007
Total receivables portfolio <sup>1</sup>	535	479
Receivables sold	300	300
Receivables retained	235	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>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Pre-tax charges	3	4	6	7
Average cost of funds <i>(per cent)</i>	4.0	4.7	4.3	4.8

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

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

<i>(millions of dollars)</i>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Depreciation	155	147	299	291
Amortization of deferred Pickering A return to service costs	4	20	33	56
Nuclear waste management costs	1	2	3	4
	160	169	335	351

Interest capitalized to construction in progress at six per cent during the three and six months ended June 30, 2008 (three and six months ended June 30, 2007 – six per cent) was \$13 million and \$26 million respectively (three and six months ended June 30, 2007 – \$10 million and \$18 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 a number of variance and deferral accounts. OPG ceased recording additions to these variance and deferral accounts as of April 1, 2008, pending a decision from the OEB in relation to its rate application that seeks approval of new payment amounts and the re-establishment of certain existing accounts. OPG will record additions to the accounts that are approved by the OEB when it receives the decision on its rate application, expected in the fall of 2008. OPG continued to amortize the Pickering A Return to Service deferral account in the second quarter of 2008 as the balance in this account is being recovered through existing rates. The balances in the other variance and deferral accounts will not be amortized until OPG receives an order from the OEB that provides recovery of these costs. OPG will continue to record interest on the unamortized balances in the variance and deferral accounts until the regulatory assets are recovered through new payment amounts or the regulatory liabilities are cleared.

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

<i>(millions of dollars)</i>	<b>June 30 2008</b>	<b>December 31 2007</b>
Regulatory assets		
Pickering A return to service costs	<b>155</b>	183
Nuclear liabilities deferral account	<b>166</b>	131
Nuclear generation development costs	<b>33</b>	28
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>369</b>	356
Regulatory liabilities		
Other	<b>13</b>	14
<b>Total regulatory liabilities</b>	<b>13</b>	14

The changes in the regulatory assets and liabilities for the six months ended June 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</b>	<b>Transmission Outages and Transmission Restrictions 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	27	-	11	5	(5)
Interest	30	3	1	-	-	-	(2)
Amortization during the year	(96)	-	-	-	-	-	-
Regulatory assets (liabilities), December 31, 2007	183	131	28	2	7	5	(14)
Increase (decrease) during the period	-	31	4	-	1	-	1
Interest	5	4	1	-	-	-	-
Amortization during the period	(33)	-	-	-	-	-	-
Regulatory assets (liabilities), June 30, 2008	<b>155</b>	<b>166</b>	<b>33</b>	<b>2</b>	<b>8</b>	<b>5</b>	<b>(13)</b>



## Nuclear Generation Development Costs

The amendments to the regulation pursuant to the *Electricity Restructuring Act, 2004* (Ontario) made in February 2007 and February 2008 clarified that OPG will recover the costs incurred and firm financial commitments made in the course of planning and preparing for the development of proposed new nuclear facilities. The amendment made in February 2008 established a deferral account for the development of proposed new nuclear facilities. This account is in place until the effective date of the OEB's first payment order. After the effective date of the OEB's first payment order, the regulation requires OPG to establish a variance account to record differences between actual non-capital costs incurred and the amount included in regulated rates for these activities. OPG will start recording costs in this variance account based on the effective date of the OEB's payment order, which is expected in the fall of 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 June 30, 2008			Three Months Ended June 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	1,385	5	1,390	1,373	3	1,376
Fuel expense	277	-	277	298	(2)	296
Operations, maintenance, and administration	750	-	750	776	5	781
Depreciation and amortization	160	(4)	156	169	(6)	163
Accretion on fixed asset removal and nuclear waste management liabilities	152	-	152	126	19	145
Property and capital taxes	24	-	24	20	1	21
Net interest expense	39	6	45	39	4	43

<i>(millions of dollars)</i>	Six Months Ended June 30, 2008			Six Months Ended June 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	2,948	9	2,957	2,897	12	2,909
Fuel expense	581	(2)	579	626	(3)	623
Operations, maintenance, and administration	1,441	4	1,445	1,470	14	1,484
Depreciation and amortization	335	(20)	315	351	(28)	323
Accretion on fixed asset removal and nuclear waste management liabilities	287	19	306	254	38	292
Property and capital taxes	30	1	31	49	2	51
Net interest expense	79	10	89	65	25	90

The OEB's decision with respect to OPG's application for new payment amounts may impact OPG's accounting for variance and deferral accounts, including the timing for recording additional amounts in these accounts and amortization of the balances in these accounts.

## 7. LONG-TERM DEBT

Long-term debt consists of the following:

<i>(millions of dollars)</i>	<b>June 30 2008</b>	<b>December 31 2007</b>
Notes payable to the Ontario Electricity Financial Corporation	<b>3,790</b>	3,665
Share of non-recourse limited partnership debt	<b>184</b>	188
	<b>3,974</b>	3,853
Less: due within one year		
Notes payable to the Ontario Electricity Financial Corporation	<b>375</b>	400
Share of limited partnership debt	<b>7</b>	7
	<b>382</b>	407
<b>Long-term debt</b>	<b>3,592</b>	3,446

Interest paid during the three months ended June 30, 2008 was \$19 million (three months ended June 30, 2007 – \$14 million), of which \$15 million relates to interest paid on long-term debt (three months ended June 30, 2007 – \$10 million). Interest paid during the six months ended June 30, 2008 was \$114 million (six months ended June 30, 2007 – \$111 million), of which \$107 million relates to interest paid on long-term debt (six months ended June 30, 2007 – \$101 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 June 30, 2008, debt financing for these projects consists of the following:

<i>(millions of dollars)</i>	<b>Niagara Tunnel</b>	<b>Portlands Energy Centre</b>	<b>Lac Seul Hydroelectric Generating Station</b>
Debt financing, as at December 31, 2007	240	210	20
New borrowing	70	55	-
<b>Debt financing, as at June 30, 2008</b>	<b>310</b>	<b>265</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 has 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 June 30, 2008, no commercial paper was outstanding (December 31, 2007 – nil), 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 June 30, 2008, there was no borrowing under this credit facility.

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

<i>(millions of dollars)</i>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Interest on long-term debt	58	49	114	99
Interest on short-term debt	4	5	7	11
Interest income	(4)	(1)	(6)	(2)
Capitalized interest	(13)	(10)	(26)	(18)
Other	(6)	(4)	(10)	(25)
Net interest expense	39	39	79	65

### 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>	June 30 2008	December 31 2007
Liability for nuclear used fuel management	6,072	5,938
Liability for nuclear decommissioning and low and intermediate level waste management	4,935	4,843
Liability for non-nuclear fixed asset removal	180	176
Fixed asset removal and nuclear waste management liability	11,187	10,957

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

<i>(millions of dollars)</i>	June 30 2008	December 31 2007
Liability, beginning of period	10,957	10,520
Increase in liability due to accretion	306	582
Increase in liability due to nuclear used fuel and nuclear waste management variable expenses	19	76
Liabilities settled by expenditures on waste management	(95)	(200)
(Decrease) in the liability for non-nuclear fixed asset removal	-	(21)
Liability, end of period	11,187	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 June 30, 2008 and December 31, 2007 consist of the following:

<i>(millions of dollars)</i>	Fair Value	
	June 30 2008	December 31 2007
Decommissioning Fund	4,993	5,075
Due to Province – Decommissioning Fund	-	(3)
	<b>4,993</b>	<b>5,072</b>
Used Fuel Fund <sup>1</sup>	4,885	4,702
Due to Province – Used Fuel Fund	(339)	(511)
	<b>4,546</b>	<b>4,191</b>
	<b>9,539</b>	<b>9,263</b>

<sup>1</sup> The Ontario NFWA Trust represented \$1,373 million as at June 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 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 six months ended June 30, 2008 and 2007:

<i>(millions of dollars)</i>	Three Months Ended June 30		Six Months Ended June 30	
	2008	2007	2008	2007
As Stated:				
Future income tax expense (recovery)	4	-	(162)	9
Future income tax: Other comprehensive income – Upon transition	-	-	-	16
Future income tax: Other comprehensive income – for the period	(1)	7	(7)	-
Liability method <sup>1</sup> :				
Future income tax expense (recovery)	17	24	(47)	51
Future income tax: Other comprehensive income – Upon transition	-	-	-	12
Future income tax: Other comprehensive income – for the period	(2)	13	(11)	8

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 June 30, 2008 and December 31, 2007:

<i>(millions of dollars)</i>	<b>June 30, 2008</b>		<b>December 31, 2007</b>	
	<b>As Stated<sup>1</sup></b>	<b>Liability Method<sup>1</sup></b>	<b>As Stated<sup>1</sup></b>	<b>Liability Method<sup>1</sup></b>
Future income tax assets – current	<b>7</b>	<b>32</b>	12	39
Long-term future income tax assets	<b>57</b>	-	-	-
Long-term future income tax liabilities	-	<b>(514)</b>	(217)	(680)

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

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 are 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*. Recently, the outstanding tax matters related to the 1999 tax audit were resolved. As a result, OPG reduced its income tax liability by \$106 million.

The amount of cash income taxes paid during the three months ended June 30, 2008 was \$30 million (three months ended June 30, 2007 – \$15 million). For the six months ended June 30, 2008, cash income taxes paid were \$30 million (six months ended June 30, 2007 - \$52 million).

## 11. PENSION AND OTHER POST EMPLOYMENT BENEFIT COSTS

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

<i>(millions of dollars)</i>	<b>Three Months Ended June 30</b>		<b>Six Months Ended June 30</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
Registered pension plan	<b>47</b>	60	<b>94</b>	121
Supplementary pension plans	<b>4</b>	3	<b>8</b>	7
Other post employment benefits	<b>55</b>	58	<b>110</b>	115

## 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. 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 June 30, 2008:

<b>Financial Instruments</b> <sup>1</sup> <i>(millions of dollars)</i>	<b>Designated Category</b>	<b>Fair Value</b>
Cash and cash equivalents	Held-to-maturity	365
Long-term investments <sup>2</sup>	Held-to-maturity	40
Nuclear fixed asset removal and nuclear waste management funds	Held-for-trading	9,539
Long-term debt (including current portion)	Other liabilities	4,030
Other commodity derivative instruments included in current and long-term accounts receivable <sup>3</sup>	Held-for-trading	20
Other commodity derivative instruments included in current and long-term accounts payable <sup>3</sup>	Held-for-trading	(30)

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

<sup>2</sup> Excludes investments of \$45 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 a third party 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 June 30, 2008:

<b>Credit Rating</b> <sup>1</sup>	<b>Number of Counterparties</b> <sup>2</sup>	<b>Potential Exposure for Largest Counterparties</b>		
		<b>Potential Exposure</b> <sup>3</sup> <i>(millions of dollars)</i>	<b>Number of Counterparties</b>	<b>Counterparty Exposure</b> <i>(millions of dollars)</i>
Investment grade	23	100	4	55

<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 Independent Electricity System Operator ("IESO") administered spot market. Net credit exposure to the IESO at June 30, 2008 was \$235 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 is to a diverse group of generally high quality counterparties. OPG's allowance for doubtful debts at June 30, 2008 was less than \$1 million.

OPG also enters into financial transactions with high rated financial institutions in order to hedge interest rate and currency exposures. At June 30, 2008, the credit exposure with these counterparties was under \$20 million. 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 bond rating agency in accordance with a minimum investment quality standard.

In regards 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 ensure, as far as possible, that the Company will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

The table below summarizes the maturity profile of the Company's long-term debt at June 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	1,644
Interest on long-term debt	212	179	131	102	439

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. Details on the Company's forward currency contracts outstanding as at June 30, 2008 are discussed below.

## 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 for long-term borrowings by entering into forward start interest rate contracts and floating-to-fixed interest rate swap contracts.

Details of the notional principal amounts and remaining terms of the interest rate contracts outstanding are disclosed below.

## 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 June 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)</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	-	5
Electricity price – Hedge <sup>2</sup>		n/a	2
Electricity price – Trading <sup>2</sup>		4	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 of Ontario (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 June 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>June 30 2008</b>
S&P/TSX Capped Composite Index	<b>13</b>
S&P 500	<b>5</b>
MSCI EAFE Index	<b>5</b>
MSCI World Index	<b>6</b>
	<b>29</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 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 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</b>	<b>Terms</b>	<b>Fair Value</b>	<b>Notional Quantity</b>	<b>Terms</b>	<b>Fair Value</b>
	<b>June 30, 2008</b>			<b>December 31, 2007</b>		
Electricity derivative instruments	<b>1.4 TWh</b>	<b>1-3 yrs</b>	<b>12</b>	1.8 TWh	1-3 yrs	35
Foreign exchange derivative instruments	<b>U.S. \$50</b>	<b>Apr./09</b>	<b>2</b>	U.S. \$48	Sep./08	(1)
Floating to fixed interest rate hedges	<b>42</b>	<b>1-11 yrs</b>	<b>(3)</b>	43	1-11 yrs	(2)
Forward start interest rate hedges	<b>472</b>	<b>1-12 yrs</b>	<b>(21)</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 June 30, 2008 and December 31, 2007 was U.S. \$1.01 and \$0.99, respectively 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 \$8 million related to derivative instruments qualifying for hedge accounting were recognized in net income during the six months ended June 30, 2008. This amount was previously recorded in other comprehensive income. Existing net gains of \$4 million deferred in accumulated other comprehensive income at June 30, 2008 are expected to be reclassified to net income within the next 12 months.

In the second 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 gain of \$4 million was reclassified to net income in the second 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 June 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>5.0 TWh</b>	<b>20</b>	9.9 TWh	14
Liabilities	<b>3.3 TWh</b>	<b>(30)</b>	1.2 TWh	(10)
		<b>(10)</b>		2
Market liquidity reserve		<b>(19)</b>		(2)
<b>Total</b>		<b>(29)</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 decreased trading revenue by \$8 million during the three months ended June 30, 2008 (three months ended June 30, 2007 – increase by \$1 million). During the six months ended June 30, 2008, the reserves decreased trading revenue by \$17 million (six months ended June 30, 2007 – nil).

### 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.

For the regulated business, OPG has filed an application with the OEB based on a proposed deemed capital structure of 42.5 per cent debt and 57.5 per cent equity.

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

(millions of dollars)	June 30 2008	December 31 2007
Long-term debt due within one year	382	407
Long-term debt	3,592	3,446
Letters of credit	205	205
Total debt	4,179	4,058
Total shareholder's equity	7,034	6,807
Total capitalization	11,213	10,865
Total debt to total capitalization	37%	37%

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

### 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 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.

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 June 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 six months ended June 30, 2008 and the year ended December 31, 2007 are as follows:

<i>(millions of dollars)</i>	<b>June 30 2008</b>	<b>December 31 2007</b>
Liability, beginning of the period	<b>100</b>	40
Increase to provision during the period	<b>122</b>	227
Payments made during the period	<b>(96)</b>	(167)
Liability, end of period	<b>126</b>	100

## 16. BUSINESS SEGMENTS

Segment (Loss) Income for Three Months Ended June 30, 2008 <i>(millions of dollars)</i>	Regulated		Unregulated			Total
	Nuclear	Hydro-electric	Hydro-electric	Fossil-Fuelled	Other	
Revenue	593	191	282	359	15	1,440
Revenue limit rebate	-	-	(3)	(52)	-	(55)
	593	191	279	307	15	1,385
Fuel expense	36	67	30	144	-	277
Gross margin	557	124	249	163	15	1,108
Operations, maintenance and administration	535	24	47	132	12	750
Inter-segment service fee	7	-	-	3	(10)	-
Depreciation and amortization	95	16	16	24	9	160
Accretion on fixed asset removal and nuclear waste management liabilities	150	-	-	2	-	152
Earnings on nuclear fixed asset removal and nuclear waste management funds	(108)	-	-	-	-	(108)
Property and capital taxes	10	3	4	4	3	24
(Loss) income before interest and income taxes	(132)	81	182	(2)	1	130

Segment Income (Loss) for Three Months Ended June 30, 2007 <i>(millions of dollars)</i>	Regulated		Unregulated			Total
	Nuclear	Hydro-electric	Hydro-electric	Fossil-Fuelled	Other	
Revenue	632	179	197	345	40	1,393
Revenue limit rebate	-	-	(1)	(19)	-	(20)
	632	179	196	326	40	1,373
Fuel expense	33	67	20	178	-	298
Gross margin	599	112	176	148	40	1,075
Operations, maintenance and administration	504	50	59	152	11	776
Inter-segment service fee	6	1	1	2	(10)	-
Depreciation and amortization	100	18	17	21	13	169
Accretion on fixed asset removal and nuclear waste management liabilities	124	-	-	2	-	126
Earnings on nuclear fixed asset removal and nuclear waste management funds	(209)	-	-	-	-	(209)
Property and capital taxes	9	2	1	5	3	20
Income (loss) before interest and income taxes	65	41	98	(34)	23	193

<b>Segment (Loss) Income for Six Months Ended June 30, 2008</b> <i>(millions of dollars)</i>	<b>Regulated</b>		<b>Unregulated</b>			<b>Total</b>
	<b>Nuclear</b>	<b>Hydro-electric</b>	<b>Hydro-electric</b>	<b>Fossil-Fuelled</b>	<b>Other</b>	
Revenue	1,358	369	526	780	37	3,070
Revenue limit rebate	-	-	(27)	(95)	-	(122)
	1,358	369	499	685	37	2,948
Fuel expense	77	116	53	335	-	581
Gross margin	1,281	253	446	350	37	2,367
Operations, maintenance and administration	1,028	47	90	252	24	1,441
Inter-segment service fee	14	1	2	4	(21)	-
Depreciation and amortization	201	32	36	46	20	335
Accretion on fixed asset removal and nuclear waste management liabilities	283	-	-	4	-	287
Earnings on nuclear fixed asset removal and nuclear waste management funds	(57)	-	-	-	-	(57)
Property and capital taxes	3	6	4	11	6	30
(Loss) income before other gains and losses	(191)	167	314	33	8	331
Other (gains) and losses	-	-	-	(2)	9	7
(Loss) income before interest and income taxes	(191)	167	314	35	(1)	324

<b>Segment Income for Six Months Ended June 30, 2007</b> <i>(millions of dollars)</i>	<b>Regulated</b>		<b>Unregulated</b>			<b>Total</b>
	<b>Nuclear</b>	<b>Hydro-electric</b>	<b>Hydro-electric</b>	<b>Fossil-Fuelled</b>	<b>Other</b>	
Revenue	1,314	355	419	858	67	3,013
Revenue limit rebate	-	-	(32)	(84)	-	(116)
	1,314	355	387	774	67	2,897
Fuel expense	65	119	39	403	-	626
Gross margin	1,249	236	348	371	67	2,271
Operations, maintenance and administration	995	73	100	280	22	1,470
Inter-segment service fee	14	1	2	4	(21)	-
Depreciation and amortization	216	34	35	39	27	351
Accretion on fixed asset removal and nuclear waste management liabilities	250	-	-	4	-	254
Earnings on nuclear fixed asset removal and nuclear waste management funds	(300)	-	-	-	-	(300)
Property and capital taxes	20	7	5	11	6	49
Income before interest and income taxes	54	121	206	33	33	447

<i>(millions of dollars)</i>	Regulated		Unregulated			Total
	Nuclear	Hydro-electric	Hydro-electric	Fossil-Fuelled	Other	
<b>Selected Balance Sheet Information</b>						
As at June 30, 2008						
Segment fixed assets in service, net	3,934	3,852	2,979	410	489	11,664
Segment construction in progress	221	340	124	41	349	1,075
Segment property, plant and equipment, net	4,155	4,192	3,103	451	838	12,739
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 June 30		Six Months Ended June 30	
	2008	2007	2008	2007
Accounts receivable	(16)	66	(40)	(63)
Prepaid expenses	13	11	10	(7)
Fuel inventory	(51)	8	13	111
Materials and supplies	(4)	(4)	(3)	(4)
Revenue limit rebate	55	20	122	116
Accounts payable and accrued charges	15	25	(152)	(138)
Income and capital taxes payable	(35)	10	(25)	19
	(23)	136	(75)	34

#### 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.