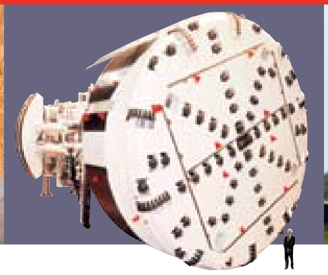
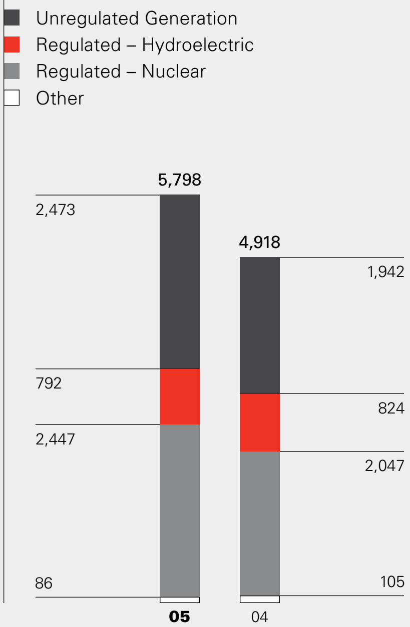
2005 Annual Report



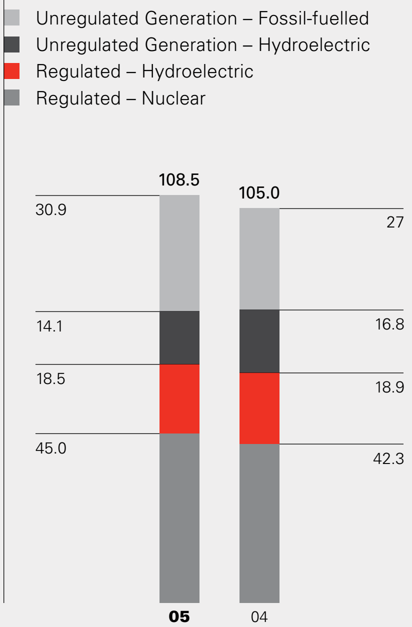
ONTARIOPOWER GENERATION

OPG 2005

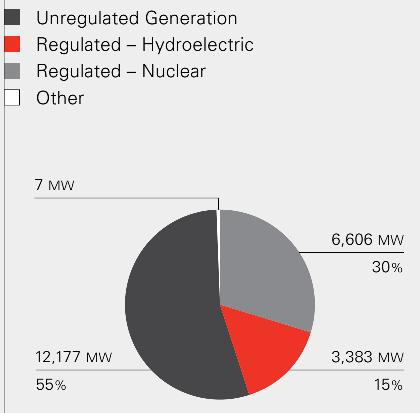
Revenue, Net of Market Power Mitigation Agreement Rebate and Revenue Limit Rebate
(millions of dollars)



Electricity Production
(TWh)



In-Service Generating Capacity by Segment
22,173 MW



Years Ended December 31 (millions of dollars)	**2005**	2004
Earnings		
Revenue before Market Power Mitigation Agreement rebate and revenue limit rebate	**6,949**	6,072
Market Power Mitigation Agreement and revenue limit rebates	**(1,151)**	(1,154)
Fuel expense	**(1,297)**	(1,153)
Gross margin	**4,501**	3,765
Operations, maintenance and administration	**2,516**	2,594
Other expenses	**1,162**	1,209
Impairment of long-lived assets	**265**	–
Income tax expense (recovery)	**118**	(80)
Extraordinary item	**74**	–
Net income	**366**	42
Cash flow		
Cash flow provided by operating activities	**1,201**	226

Contents

Corporate Profile

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.

In 2005, OPG generated 108.5 terawatt hours (TWh) of electricity.

OPG's electricity generating portfolio as of December 31, 2005, had a total in-service capacity of 22,173 megawatts (MW), which consisted of:

- three nuclear generating stations with a capacity of 6,606 MW
- five fossil-fuelled generating stations with a capacity of 8,578 MW
- 64 hydroelectric generating stations with a capacity of 6,982 MW and
- three wind generating stations (which includes a 50% interest in the Huron Wind joint venture) with a capacity of 7 MW.

In addition, OPG, ATCO Power Canada Ltd. and ATCO Resources Ltd. co-own a 580 MW gas-fired generating station near Windsor, Ontario. In November 2005, OPG's Pickering A, Unit 1 nuclear reactor was returned to service, adding 515 MW to OPG's in-service generating capacity. OPG also owns two other nuclear generating stations, which are leased on a long-term basis to Bruce Power L.P.

Electricity Terms

One megawatt (MW) is one million watts. Megawatts are a measure of electricity supply capacity at a point in time.

One kilowatt (kW) is 1,000 watts; one gigawatt (GW) is one billion watts; and one terawatt (TW) is one trillion watts.

One kilowatt hour (kWh) is a measure of electricity demand per hour by customers. One kilowatt hour is the energy expended by ten 100 watt lights burning for one hour.

The average Ontario household uses approximately 1,000 kWh per month.

One megawatt hour (MWh) is 1,000 kWh; one gigawatt hour (GWh) is one million kWh; and one terawatt hour (TWh) is one billion kWh.

On the Cover

Nelly King, Technical Engineer/Officer, OPG Nuclear Waste Management; Feeder tube inspection, Pickering A, Unit 1; tunnel boring machine similar to the one being built to dig OPG's Niagara Tunnel; Atikokan fossil-fuelled generating station, which celebrated 20 years of operation in 2005.

Select List of Accomplishments

— The Pickering A, Unit 1 is returned to service after being laid up for nearly eight years.

— OPG's Darlington nuclear station is the best performing multi-unit nuclear station in Canada for the second consecutive year.

— Official groundbreaking for the start of construction of the Niagara Tunnel takes place in Niagara Falls.

— To help meet Ontario's electricity demand during one of the hottest summers on record, OPG's fossil-fuelled stations produce 62% more electricity than in the summer of 2004.

— OPG's coal-fired plants achieve their lowest acid-gas emission rates in OPG's history.

— OPG receives Gold Award from the Electrical and Utilities Safety Association for excellence in its safety management system and safety culture.

Message from Jake Epp, Chairman

The Board of Directors is committed to ensuring that OPG continues to move forward as a commercially focused, performance-driven company – one that is consistently open, transparent and accountable in its activities. In 2005, a number of steps were taken which helped strengthen these values, enhanced our governance capability and supported the company's commitment to excellence.

A New Mandate

In the summer of 2005, OPG reached a Memorandum of Agreement with our Shareholder, the Province of Ontario, regarding our role and responsibility as a power producer in Ontario. Under this agreement, OPG has a clear mandate to operate as a commercial company focused on a number of key activities and goals:

- generating electricity in a cost effective and efficient manner;
- continuously improving our nuclear performance and benchmarking that performance against the best CANDU operators internationally and in North America;
- expanding our hydroelectric capacity;
- operating our fossil-fuelled plants according to commercial principles until they are shut down as specified by the government's coal replacement policy.

In addition, OPG will maintain its high level of accountability and transparency and will operate under the highest standards of corporate governance, social responsibility, corporate citizenship and environmental stewardship.

Our new mandate gives focus and direction to our efforts and enables the Board – and others – to measure management's progress and hold them accountable for results.

Strengthening Our Governance Capability

OPG strengthened its governance capability in 2005 by adding two new directors. George Lewis and Peggy Mulligan were appointed to the Board of Directors. Mr. Lewis is Chairman and CEO, RBC Asset Management Inc. Mrs. Mulligan is Executive Vice President and Chief Financial Officer of Linamar Corporation. The OPG Board now has a full complement of 12 directors, with experience in engineering and project management; human resources; financial management and nuclear operations.

The Governance and Nominating Committee of the Board has also led the Board in implementing charters for the Board and each of its committees; developing position descriptions for each of the Committee Chairs; and supporting the continuing education of our directors. We also instituted a comprehensive orientation program for new directors joining the Board.

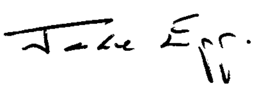
Open, Transparent and Accountable

OPG's governance, including our Board and Committee Charters, is described on the OPG web site. The web site also provides access to the Memorandum of Agreement with the Ontario government and shareholder directives. In 2005, OPG received two such directives under Section 108 of the Ontario Business Corporations Act. The first was to convert to gas our Thunder Bay coal-fired station; the second required us to amend our lease arrangement with Bruce Power.

New Leadership

In May 2005, Richard Dicerni ended his tenure as OPG's Acting President and CEO and OPG's new President and CEO, Jim Hankinson, was appointed by the Board.

On behalf of the Board, I would like to thank Richard Dicerni for his contribution to OPG and to welcome Jim Hankinson in his new role.



Message from Jim Hankinson, President and CEO

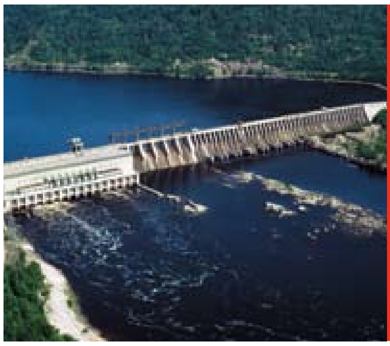
Ontario Power Generation is a performance-focused company. Performance is the yardstick we use to measure our progress; the impetus that drives our business; and the value that defines our success.

We are committed to achieving performance excellence through generation performance; asset improvement; supply expansion; and by operating in a cost effective and socially responsible manner that respects the needs of employees, the environment and communities.

In 2005, we made important strides in each of these areas while also improving our financial performance.

- Our generation performance was strong as we continued to develop and implement strategies to improve station productivity, enhance plant condition, and extend the operational lives of our stations.
- We expanded our production capacity by refurbishing and upgrading many of our generating stations – including the return to service of our Pickering A, Unit 1 nuclear reactor – as well as by launching new supply initiatives.
- We made a difficult but necessary commercial decision not to refurbish our two remaining laid-up nuclear units at Pickering A.
- We continued to achieve high levels of public safety, improved our workplace safety performance by reducing our employee injury rates, and maintained and enhanced our ongoing commitment to good governance, environmental stewardship and corporate citizenship.

In the summer of 2005, we negotiated a Memorandum of Agreement with our Shareholder, the Province of Ontario, which further sharpened our focus on these priorities and sets us on a clear direction for future growth and success.



The Otto Holden generating station. OPG manages its hydroelectric assets through prudent investments to enhance performance, increase capacity, and preserve their long-term capability. While hydroelectric production declined in 2005 due to lower water levels, the availability factor of these assets remained high at 92.4%.

The year was not without its challenges, which included a major, unplanned outage at the Pickering A nuclear station to inspect and maintain feeder tubes; the decision not to refurbish the two Pickering units; and the decommissioning of our Lakeview coal-fired station, as directed by the Ontario government.

In the following pages, I will be reviewing a number of OPG's achievements and related developments that took place during the past year. Overall, I am pleased with the progress we made in 2005. I recognize that our performance can continue to improve and am committed to making that happen with the support and contribution of all our employees.

Performing

at consistently high levels to provide electricity where and when it's needed

Darlington Nuclear Generating Station

OPG's nuclear operations had an excellent year in 2005. Nuclear production increased by more than 6%, accounting for over 28% of the electricity consumed in Ontario. For the second year in a row, the Darlington station was Canada's best performing multi-unit nuclear generating station with a unit capability factor of 90.6%.

OPG Nuclear Performance: Key Results	2005	2004
— Production (TWh)	45.0	42.3
— Capability Factor (%)	83.8	80.4
— Nuclear Performance Index	76.4	70.7
— Forced Loss Rate (%)	5.35*	7.6
— All Injury Rate (per 200,000 hours worked)	1.06	1.25

*Lower number signifies improvement

Financial Performance

I am pleased to report that OPG's financial performance improved in 2005. Net income was $366 million or $1.43 per share compared to net income of $42 million or $0.16 per share in 2004. Earnings were positively affected by an increase in gross margin caused by higher average sales prices and increased nuclear and fossil-fuelled generation. The higher average sales prices we received in 2005 were primarily due to:

- higher average Ontario spot market prices resulting from stronger electricity demand during the very hot summer and the effect of higher natural gas prices; and
- the introduction of regulated prices and other related regulatory changes on April 1, 2005.

Our improved financial performance in 2005 was also partly due to decreased operations, maintenance and administration (OM&A) expenses resulting from the deferral in 2005 of costs related to the Pickering A, Unit 1 restart project as required by regulation. These OM&A reductions were partially offset by higher nuclear maintenance related to continuing improvements in station reliability; inventory write-offs as a result of the decision not to return Pickering A Units 2 and 3 to service; and increases in pension and other post employment benefit expenses.

Our 2005 earnings were negatively affected by impairment losses on OPG's Lennox gas and oil-fired generating station and on Units 2 and 3 of the Pickering A nuclear generating station. The impairment loss on the Lennox generating station was a result of the Province's decision to allow OPG to recover only its fixed operating costs through a contractual arrangement but not the carrying value of the station. The impairment loss on Units 2 and 3 at the Pickering A nuclear generating station resulted from the decision not to return these units to service.

OPG's Moderating Impact on Electricity Prices: As our financial performance improved in 2005, OPG continued to exercise a strong moderating influence on electricity prices paid by Ontario consumers. As a result of regulated rates and rebate mechanisms, OPG received an average price of 4.9 ¢/kWh in 2005 for the electricity produced from all of its generating stations. This price was considerably less than the weighted average hourly Ontario electricity price of 7.2 ¢/kWh received by other Ontario generators in 2005. From May 2002 to March 31, 2005 OPG rebated $4 billion under the former Market Power Mitigation Agreement (MPMA) to the benefit of Ontario's electricity users. In addition, for the balance of 2005, we will rebate some $739 million as a result of a revenue cap on much of our unregulated generation that went into effect on April 1, 2005.

The Lambton fossil-fuelled genererating station near Sarnia, Ontario. Production at OPG's fossil-fuelled stations increased by 14% in 2005. At the same time, acid gas emissions at these stations were the lowest in more than two decades.

Generation Performance

OPG generated 108.5 TWh of electricity in 2005 – an increase of 3.3% over the company's 2004 production of 105 TWh.

Nuclear: OPG's nuclear generation in 2005 rose to 45 TWh, compared to 42.3 TWh in 2004. For the second year in a row Darlington was the best performing multi-unit nuclear station in Canada with a unit capability factor of 90.6%. Pickering B achieved a unit capability factor of 77.7% compared to a 69.8% unit capability in 2004. Both stations performed at high levels of reliability during the cold winter and hot summer of 2005, with forced loss rates better than target. Our Pickering A station received a five-year operating licence from the Canadian Nuclear Safety Commission (CNSC) – the longest licence period for a nuclear power reactor that the CNSC grants to date.

Fossil: OPG's fossil-fuelled plants generated 30.9 TWh of electricity in 2005. This was nearly a 14% increase over the 2004 output. Contributing factors included higher electricity demand and improved station reliablity as evidenced by the lower Equivalent Forced Outage Rate of 15.9% achieved by these stations in 2005 compared to 18.7% in 2004. The strong reliability of our fossil-fuelled plants was also due to improved performance at our Nanticoke station and to the focused efforts of its employees and the employees at all our fossil facilities. OPG's fossil-fuelled plants function largely as "swing" resources during high demand periods. When demand reached record high levels during the past summer, these plants were producing on the hottest days up to 40% of OPG's generation.

Hydroelectric: While our hydroelectric output fell somewhat compared to 2004 due to lower water levels, the reliability of our hydroelectric stations continued to be very strong throughout the year, with an availability factor of 92.4%. These valuable assets deliver a steady supply of affordable, renewable power, and represent an important part of OPG's generation mix.

OPG employees prepare to install a new rotor on Unit 14 at the Beck 2 hydroelectric station. The work was part of an extensive nine-year project to replace and upgrade station equipment. Completed in the Spring of 2005, the project adds 194 MW to OPG's hydroelectric capacity.

Asset Improvement

Nuclear: OPG's higher nuclear output in 2005 is a direct result of our commitment to improve the performance of our nuclear stations – our top operational priority. Our strategy is to operate our nuclear assets efficiently and cost effectively while investing prudently to improve their reliability, predictability and lifespan. To this end, we continued to undertake in 2005 extensive and sustained programs in areas such as steam generator inspection and rehabilitation; feeder tube integrity; pressure tube remediation; and maintenance backlog reduction. As part of this strategy, we completed the first year of our 85/5 initiative at Pickering B – a major three-year program to improve the material condition and performance of that station. The station's goal is to achieve and maintain by 2007 an 85% capacity factor and a 5% forced loss rate – while reducing its average outage duration.

These and other improvement initiatives, many of which were implemented during the planned outages we performed on four of our nuclear units in 2005, are helping to maximize the life-expectancy of our nuclear fleet and contributed to the positive performance results achieved by our nuclear plants in the past year. To ensure that our nuclear plants continue to improve, we regularly measure them against the best plants in North America with particular focus on generation performance, operational excellence, backlogs and costs. By the end of the decade, decisions will be made on whether to extend the lives of OPG's nuclear units. Achieving consistently strong performance from our nuclear assets will help influence those decisions.

Fossil: While the Ontario government is committed to closing these plants over a period from 2007 to 2009, it has said it will not do so at the expense of supply reliability. Until they are shut down, however, we will continue to operate our coal plants in an efficient, reliable and environmentally responsible manner. Our goal is to ensure that the condition of our coal-fired plants is as good, if not better, on the day they close as it is today.

Hydroelectric: Our strategy with respect to our hydroelectric plants is to invest in them on an ongoing basis to enhance their performance, extend their service lives and reduce operational costs. Our improvements include replacing aging equipment, runner upgrades, station automation and innovative maintenance practices. A major milestone in this area was reached in 2005 with the completion of a nine-year rehabilitation initiative at the Beck 2 hydroelectric station near Niagara Falls, which added 194 MW to OPG's hydroelectric capacity. Additional hydroelectric upgrades between 2006 and 2015 will add another 150 MW to OPG's capacity.

These OPG employees are representatives of key groups involved in Pickering B's Spacer Location and Repositioning (SLAR) program. The SLAR program helps avoid pressure tube damage by preventing a nuclear reactor's pressure tubes from coming into contact for extended periods of time with its calandria tubes. By the end of 2005, about 83% of Pickering B's 1,565 fuel channels had been inspected using SLAR.

Improving

our assets to ensure reliability

Pickering A, Unit 1

Standing before the reactor face of the Pickering A, Unit 1 nuclear reactor, two inspectors study the ends of the 390 pressure tubes that hold fuel for the reactor. OPG's successful return to service of Unit 1 in 2005 was one of the largest and most complex projects ever undertaken by the company. Off-line for almost eight years, the newly refurbished reactor adds to Ontario's electricity supply 515 MW of much-needed capacity that is virtually free of emissions that contribute to smog and global warming.

Unit 1 Refurbishment Achievements

- 2,879 peak employment
- 1.9 million hours worked
- 2.9 million individual parts installed
- 204 kilometres of new electrical cable
- 26,402 metres of pipe
- 24,500 individual tasks completed
- More than 5 million hours worked without a Lost Time Accident

Expanding

our generation capacity to help meet Ontario's energy needs

Niagara Tunnel Project

Ontario requires clean, reliable hydroelectric power for the future. Our mandate calls on us to help provide that power by developing and investing in Ontario's hydroelectric potential. The Niagara Tunnel is a major initiative on the road to this goal. In 2005, the OPG Board approved the total project and the award of the Design/Build contract to Strabag AG. Construction is currently underway. When complete, it will carry an additional 500 cubic metres per second of water from above Niagara Falls to OPG's Sir Adam Beck Generating Complex at Queenston, enabling more clean, renewable energy to be generated from the Niagara River while continuing to preserve the natural beauty of the Falls themselves.

Niagara Tunnel at a Glance

- 10.4 kilometres long
- $985 million estimated cost
- 350 peak employment
- 2009 completion date
- 90 years operating life
- 1.6 billion kilowatt hours of additional renewable energy per year

New Supply Initiatives

In addition to improving our performance, OPG is also investing in new generation capacity. Forecasts indicate that within the next several years Ontario could face electricity supply shortfalls without significant new generation initiatives. While OPG is not responsible for meeting all of Ontario's electricity supply needs, we have undertaken a number of new supply initiatives which help address this challenge. These initiatives will also help us to fulfill an important part of our mandate – which is to expand, develop and improve our hydroelectric generation capacity.

Our initiatives in this area include the construction launch of a new 10.4 kilometre tunnel to divert more water to the Beck hydroelectric stations. This initiative will increase the average annual energy output of these facilities by about 14% and is one of our most significant and exciting capital projects.

OPG also received Board approval to construct a new 12.5 MW hydroelectric generating station at Lac Seul in Northwestern Ontario. This construction is now underway.

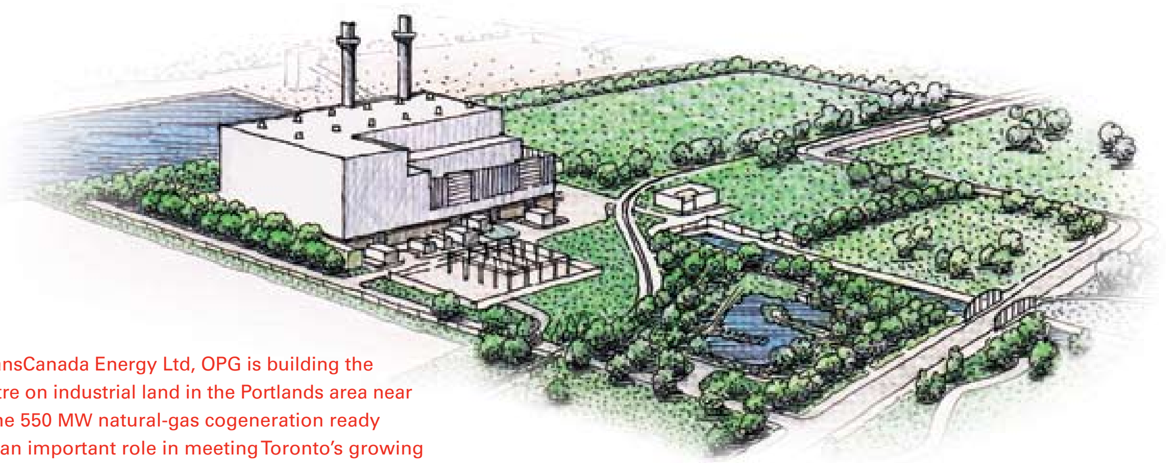
In addition to these projects, we are investigating options for the redevelopment of four hydroelectric plants in the Lower Mattagami River system in Northeastern Ontario. This initiative has the potential to contribute between 150 MW to 450 MW of additional clean, renewable hydroelectric power to the Province's electricity supply.

Complementing our hydroelectric initiatives, we are constructing, in partnership with TransCanada Energy Ltd., the Portlands Energy Centre – a 550 MW combined cycle natural-gas and co-generation capable generating facility located in downtown Toronto.

Under construction in Northwestern Ontario, the Lac Seul Generating Station will add 12.5 MW to OPG's hydroelectric capacity. The $47 million project is expected to be finished in 2007. The station will use much of the water currently being spilled at the adjacent Ear Falls hydroelectric station, increasing the overall efficiency of the site.

Finally, the Pickering A, Unit 1 restart – while one of our major refurbishment and asset improvement successes – was also our most notable new supply initiative, adding 515 MW of baseload power to our capacity. This massive and complex project confirmed OPG's ability to deliver a major capital project and represented a major accomplishment for the company in 2005. I want to thank all OPG employees who made this achievement possible.

Effective Cost Management: Cost management is a critical priority for OPG, and we employ a variety of cost management initiatives. Over the past few years, we reduced by some 20% our executive ranks and our corporate support groups. On the operating side, we are investing directly in our plants to improve their performance through programs such as the 85/5 initiative at Pickering B, upgrades to our hydroelectric stations and benchmarking programs to identify improvement opportunities. Changes in the way we blend different types of coal to fuel our Nanticoke station resulted in significant cost savings in 2005 and going forward.



In partnership with TransCanada Energy Ltd, OPG is building the Portlands Energy Centre on industrial land in the Portlands area near downtown Toronto. The 550 MW natural-gas cogeneration ready power plant will play an important role in meeting Toronto's growing energy needs. Ontario's Independent Electricity System Operator has estimated that the city will need 500 MW of new capacity by 2010, even with conservation initiatives being planned.

Employee-mentors at Nanticoke GS with co-op students. In 2005, Nanticoke received a "Passport to Prosperity" award from the Grand Erie Training and Adjustment Board. The award recognizes Nanticoke's efforts in providing co-op work opportunities for more than 350 high school students since 1991.

Operating to the Highest Corporate Standards

Safety Performance: Among our many priorities as a power provider, none is more important than ensuring the safety of the public and our employees at all times. This principle is rigorously applied at all our facilities.

OPG's nuclear plants operate according to strict regulatory standards and codes. In 2005, radiation emissions at both our Pickering and Darlington facilities continued to be a very small fraction of what Canadians receive annually from naturally occurring sources and much lower than that permitted by regulation. Since the Canadian nuclear power industry's inception over 40 years ago, no member of the public has ever been harmed as a result of radiation from our nuclear plants or waste management facilities. OPG's nuclear plants will continue to live up to these high standards.

We are equally committed to public safety at our other facilities. OPG's Public Water Safety Program is designed to help ensure that our hydroelectric stations and dams are operated safely and have the appropriate control measures in place to protect the public. Fundamental to this program is its focus on making the public in our site communities, including tourists, aware of the dangers associated with OPG's dams, hydroelectric stations and surrounding waterways. The uniqueness of each of our hydroelectric sites, the geographical diversity of the site communities themselves, and the large number of people who use the waterways where we operate make this a huge challenge. But it is one that we are committed to meeting.

With respect to employee safety, our goal is zero workplace injuries; and we continue to make progress toward meeting that ambitious target.

- Our 2005 All Injury Rate (AIR) of 1.33 injuries per 200,000 hours worked was better than the top quartile threshold (three year rolling average) set by the Canadian Electricity Association (CEA) and 13% better than our AIR performance in 2004.
- Our 2005 Accident Severity Rate (ASR) of 2.03 days lost per 200,000 hours was not as strong as our 2004 performance, but still well within the CEA's top quartile threshold (three year rolling average).

OPG's consistently strong workplace safety performance is a direct result of a vigorous safety culture that we have adopted at all our facilities. Employees are taught and encouraged to build safety behaviours into all aspects of their work and to take personal ownership of their own safety and that of their co-workers. This Internal Responsibility System is a cornerstone of our safety success.

Our safety commitment extends to our contractors, whom we expect to work to high safety standards, and we continued to implement programs requiring them to do so. We also continued our focus on promoting strong safety behaviours among young OPG employees and young people in the communities where we operate and across Ontario. In recognition of our efforts in building a strong safety management system and culture, the Electrical and Utilities Safety Association awarded OPG its Gold Award in 2005. OPG was the first recipient of this award.

Environment: As a major generating company with facilities across Ontario, we recognize that we have an impact on the environment and strive to minimize that impact at all times. Our coal-fired plants, for example, had the lowest acid-gas emission-rates in OPG's history even though they produced significantly more energy than in 2004. This strong and positive environmental performance was due in part to our sustained investments in clean air technology – including selective catalytic reduction equipment, combustion improvements, and the use of lower sulphur fuels.

(Left to right) John McCann, Manager, Lennox GS; OPG employee Liisa Blimkie, Ottawa-St. Lawrence Environment, Chemical and Safety Technician; and Leeds County Stewardship Council's Dwayne Struthers, with Peregrine falcon chicks at Charleston Lake. OPG staff worked with the Leeds County Stewardship Council, the Canadian Peregrine Foundation and the Charleston Lake Environmental Foundation to enable the falcons to be released into the wild.

Respecting

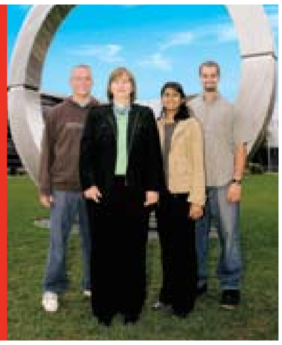
the needs of employees,
the environment
and the community

Darlington Mechanical Maintainers Skills Training

Mechanical maintainers at the Darlington nuclear station learn how to apply safe behaviours and procedures to protect themselves from workplace falls. Achieving zero workplace injuries is the ultimate goal of OPG's safety programs. The company's strong commitment to workplace safety was reflected in many notable safety initiatives and successes during 2005.

Select Accomplishments

- Continued top quartile safety performance within the electrical industry
- Continued operation of site-based Occupational Health & Safety Assessment Series 18001 safety management systems
- Launch of OPG-wide "Keep Your Promise" campaign, highlighting how our employees keep their promise to work safely
- Broadening of our Health & Safety Policy to include an emphasis on young worker safety within OPG, in communities where we operate, and across Ontario



Students at the University of Ontario Institute of Technology (UOIT). Located in Ontario's Durham Region, UOIT places a strong emphasis on science and technology education and career-focused learning. OPG is investing $10 million over a five year period in UOIT to contribute to the educational strength of Durham Region and help meet the need for highly-qualified, technically trained young employees.

For the third year in a row, OPG had no major impact spills. We also reported no moderate impact spills, continued to reduce our total amount of acid gas emissions, and planted an additional 326,000 native trees and shrubs in Ontario to help offset carbon dioxide emissions – for a total of 2.2 million trees planted since 2000 as part of our biodiversity commitment.

In addition, the environmental management systems at OPG's nuclear, hydroelectric and fossil plants were all recertified in 2005 under the internationally recognized ISO 14001environmental management standard. We also were recognized for our efforts in protecting and helping to restore the natural habitats that surround many of our generating facilities. As examples, the Darlington nuclear station was nominated for the Corporate Habitat of the Year Award by the Wildlife Habitat Council (WHC), and our Lennox generating station was nominated for the WHC's Rookie of the Year award. Currently, seven OPG sites are certified under the WHC for their wildlife habitat programs.

OPG also set aside $454 million in segregated funds to cover the future costs of decommissioning our nuclear plants and safely storing their used nuclear fuel. By the end of 2005, these funds totalled about $7 billion against a total present value liability of about $8.5 billion, helping to ensure that future generations of Ontarians will not be burdened with this cost.

Corporate Citizenship: OPG's corporate citizenship commitment embraces a wide range of endeavours. We communicate frequently with the communities where we operate through newsletters; reports to municipal councils; open houses; and door-to-door visits by employees to provide local residents with information about OPG. These outreach activities underscore our commitment to be an open, transparent and accountable corporate citizen.

We also continued to support many local initiatives in the communities where we operate. We focus on educational, environmental and community initiatives that enhance the quality of life in these communities. We provide assistance for student awards; engineering, science and technology based projects; youth amateur sports; biodiversity programs; community festivals; health and safety initiatives; and humanitarian efforts such as food banks and shelters. In 2005, OPG helped support 755 such initiatives in these and similar areas though our Corporate Citizenship Program.

In addition, OPG employees and pensioners contributed $1.8 million to the company's annual Charity Campaign, whose proceeds go to charities across Ontario. Our employees and pensioners also are active as volunteers, freely offering their time and services to community groups and causes.

Employees: This past year, I took the opportunity to travel across Ontario meeting personally with the men and women who run OPG's facilities. As I travelled from site to site talking to employees, I was continually impressed by their knowledge, experience, professionalism, and commitment.

OPG's 11,000 employees are the backbone of the company and a major reason for our success. Our goal is to be an organization whose performance and values consistently enable our employees to be engaged, productive and proud members of the OPG team. We made progress toward this goal in 2005. Employee engagement scores rose significantly in many parts of the company – thanks in part to the committed efforts of many OPG managers and supervisors.

In 2005 and early 2006, we also successfully renewed collective agreements with the two unions representing most of our employees – the Power Workers' Union and the Society of Energy Professionals. Both agreements are long-term in duration and were reached without the assistance of a mediator or arbitrator. The success of these negotiations reflects the mature and positive relationship that exists between OPG and its unions. These agreements also provide employees and OPG with the stability and flexibility we need to meet the challenges and opportunities that await us in the future. I have every confidence that our future is going to be bright, exciting and successful.

Management's Discussion and Analysis

Contents

This Management's Discussion and Analysis ("MD&A") should be read in conjunction with the audited consolidated financial statements and accompanying notes of Ontario Power Generation Inc. ("OPG" or the "Company") as at and for the year ended December 31, 2005. 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 February 8, 2006.

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, nuclear decommissioning and waste management, closure of coal-fired generating stations, pension and other post employment benefit ("OPEB") obligations, income taxes, spot market electricity prices, the ongoing evolution of the Ontario electricity industry, environmental and other regulatory requirements, and the weather. Accordingly, undue reliance should not be placed on any forward-looking statement.

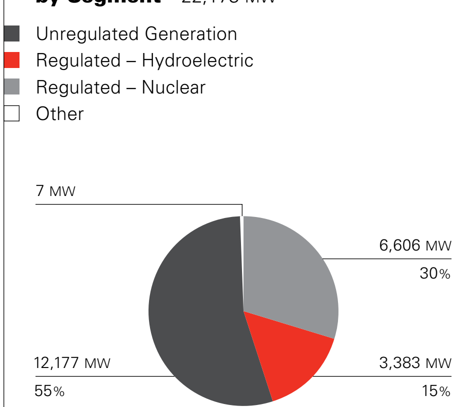
The Company

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 created under the *Business Corporations Act* (Ontario) and is wholly owned by the Province of Ontario (the "Province").

At December 31, 2005, OPG had 22,173 megawatts (MW) of in-service generating capacity. OPG's electricity generating portfolio consisted of three nuclear generating stations, five fossil-fuelled generating stations, 64 hydroelectric generating stations and three wind generating stations (which includes a 50 per cent interest in the Huron Wind joint venture). In addition, OPG, ATCO Power Canada Ltd. and ATCO Resources Ltd. co-own a gas-fired generating station. All four units of the Pickering A nuclear generating station were laid up in 1997. Unit 4 was returned to service in 2003 and Unit 1 was returned to service in November 2005, adding 515 MW to OPG's in-service generating capacity. OPG also owns two other nuclear generating stations, which are leased on a long-term basis to Bruce Power L.P. ("Bruce Power").

Effective April 1, 2005, the output from most of OPG's baseload hydroelectric facilities and all of its nuclear facilities became rate regulated. OPG continues to receive the spot market price for the output from its remaining hydroelectric, fossil-fuelled and wind generating stations, subject to a revenue limit. With the introduction of rate regulation, OPG revised its reporting segments to separately reflect the regulated and unregulated aspects of its operations. OPG's operating results are reported on a consolidated basis as well as by business segment. These segments are: Regulated – Nuclear, Regulated – Hydroelectric, and Unregulated Generation.

In-Service Generating Capacity by Segment 22,173 MW



Rate Regulation

A regulation was introduced pursuant to the *Electricity Restructuring Act, 2004,* which provides that, effective April 1, 2005, OPG receives regulated prices for electricity generated from most of its baseload hydroelectric and all of its nuclear facilities. This includes electricity generated from 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 regulated price received by OPG for the first 1,900 megawatt hours (MWh) of production from the regulated hydroelectric facilities in any hour is $33.00/MWh (3.3¢/kWh). As an incentive to encourage maximum hydroelectric production during peak demand periods, any production from these regulated hydroelectric facilities above 1,900 MWh in any hour receives the Ontario electricity spot market price. The regulated price received by OPG for production from the nuclear facilities is $49.50/MWh (4.95¢/kWh). These regulated prices were established by the Province, based on forecast production volumes and total operating costs, including the cost of capital and assuming an average five per cent return on equity. These initial prices took effect April 1, 2005, and are expected to remain in effect until at least March 31, 2008, at which time it is anticipated that the Ontario Energy Board ("OEB") will establish new regulated prices. If there are changes to the fundamental assumptions on which these regulated prices were developed, they may be amended by the Province.

The regulation directed OPG to establish variance accounts for costs incurred on or after April 1, 2005 that are associated with differences in hydroelectric electricity production due to differences between forecast and actual water conditions; changes in nuclear electricity production due to unforeseen changes to the law or to unforeseen technological changes; changes to revenues assumed for ancillary revenues from the regulated facilities; acts of God (including severe weather events); and transmission outages and transmission restrictions. In addition, the regulation directed OPG to establish a deferral account for Pickering A return to service non-capital costs incurred on or after January 1, 2005.

The production from OPG's other generating assets remains unregulated and continues to be sold at the Ontario electricity spot market price. However, 85 per cent of the generation output from OPG's other generating assets, excluding the Lennox generating station, Transition – Generation Corporation Designated Rate Options ("TRO") volumes and forward sales as of January 1, 2005, are subject to a revenue limit based on an average price of $47.00/MWh (4.7¢/kWh). This revenue limit was originally established for a period of 13 months ending April 30, 2006. The Ontario Government ("Government") has recently announced the extension of the revenue limit for an additional three years. Starting May 1, 2006, the revenue limit will decrease to 4.6¢/kWh from the present limit of 4.7¢/kWh. On May 1, 2007, the revenue limit will return to 4.7¢/kWh and increase to 4.8¢/kWh effective May 1, 2008. Revenues above these limits will be returned to the Independent Electricity System Operator ("IESO"), and the IESO will subsequently issue a rebate to consumers.

The implementation of regulated pricing for the generation from OPG's baseload hydroelectric and nuclear facilities, as well as the revenue limit on OPG's unregulated generating assets, replaced OPG's rebate obligations under the Market Power Mitigation Agreement effective April 1, 2005.

Highlights/Executive Summary

This section provides an overview of OPG's consolidated operating results. A detailed review of OPG's performance by business segment is included in a later section.

2005 Earnings

OPG's earnings improved in 2005 following the implementation of the regulatory changes which took effect April 1, 2005. Earnings from OPG's assets that are now regulated improved in 2005 compared to 2004 as a result of the introduction of regulated prices that reflect the projected production and costs of operations, including a cost of capital with an average five per cent return on equity, and the corresponding elimination of the Market Power Mitigation Agreement rebate. Earnings from OPG's unregulated assets also improved in 2005. While a significant portion of OPG's output from its unregulated assets was subject to the revenue limit, this limit was higher than the limit that was prescribed under the Market Power Mitigation Agreement.

Over the May 1, 2002 to March 31, 2005 period, OPG's earnings and liquidity were severely impacted by the requirement to rebate a significant portion of its revenues under the Market Power Mitigation Agreement. In total, the Market Power Mitigation Agreement rebate amounted to $4 billion over this period.

(millions of dollars)	**2005**	2004
Revenue		
Revenue before Market Power Mitigation Agreement and revenue limit rebates	**6,949**	6,072
Market Power Mitigation Agreement rebate	**(412)**	(1,154)
Revenue limit rebate	**(739)**	–
	5,798	4,918
Earnings		
Income (loss) before impairment of long-lived assets, income taxes and extraordinary item	**823**	(38)
Impairment of long-lived assets	**265**	–
Income (loss) before income taxes and extraordinary item	**558**	(38)
Income tax expense (recovery)	**118**	(80)
Income before extraordinary item	**440**	42
Extraordinary item	**74**	–
Net income	**366**	42
Electricity generation (TWh)	**108.5**	105.0
Cash flow		
Cash flow provided by operating activities	**1,201**	226

Net income for the year ended December 31, 2005 was $366 million compared to a net income of $42 million in 2004, an increase in earnings of $324 million. Income before income taxes and an extraordinary item for the year ended December 31, 2005 was $558 million compared to a loss of $38 million in 2004, an increase of $596 million. During 2005, OPG recorded a one-time extraordinary loss of $74 million to reflect the impact of adopting rate regulated accounting for income taxes effective April 1, 2005.

The following is a summary of the factors impacting OPG's results for 2005 compared to 2004, on a before-tax basis:

(millions of dollars – before tax)	
Loss before income taxes for the year ended December 31, 2004	**(38)**
Changes in gross margin	
Increase in electricity sales prices after Market Power Mitigation Agreement rebate and revenue limit rebate	662
Change in electricity generation by segment:	
Regulated – Nuclear	138
Regulated – Hydroelectric	(14)
Unregulated – Hydroelectric	(116)
Unregulated – Fossil-fuelled	62
Other changes in gross margin	4
	736
Decrease in Pickering A return to service OM&A expense due to deferral of non-capital costs in 2005 as a rate regulated asset	267
Increase in OM&A costs due to write-off of inventory, as a result of not returning Pickering A generating station Units 2 and 3 to service	(57)
Increase in nuclear maintenance and repairs	(101)
Increase in pension and other post employment benefit costs	(47)
Increase in earnings on nuclear fixed asset removal and nuclear waste management funds	68
Other net changes	(5)
Increase in income before income taxes and extraordinary item, excluding impairment of long-lived assets	**861**
Impairment of Pickering A generating station Units 2 and 3	(63)
Impairment of Lennox generating station	(202)
Income before income taxes and extraordinary item for the year ended December 31, 2005	**558**

Earnings for the year ended December 31, 2005 were significantly impacted by an increase in gross margin from electricity sales due primarily to higher average sales prices compared to 2004. The increase in OPG's average sales price was due in part to higher average Ontario spot market prices, which impacted revenue from OPG's unregulated generating assets, and the introduction of regulated prices and other related regulatory changes effective April 1, 2005. The higher spot market prices were primarily due to higher demand resulting from a prolonged period of hot summer weather and the effect on electricity prices of higher natural gas prices. Higher electricity generation in 2005 compared to 2004 due to higher demand and improved station performance also contributed to an increase in gross margin.

The increase in income during 2005 was also due to a decrease in operations, maintenance and administration ("OM&A") expenses resulting from the deferral of non-capital costs related to the Pickering A return to service project, commencing January 1, 2005, as required by a regulation pursuant to the *Electricity Restructuring Act, 2004*.

The favourable impact of these changes was partly offset by an impairment loss on OPG's Lennox generating station of $202 million before tax. It was determined that the Lennox generating station, as a relatively high variable cost plant, would not be able to recover its fixed operating costs and carrying value from the wholesale electricity market in the future. OPG had initiated discussions with the Province, with the expectation of entering into a contractual arrangement for the recovery of the annual fixed operating costs and the carrying value of the Lennox generating station. OPG was subsequently advised by the Province during the first quarter of 2005 that it would continue to support OPG in negotiating an arrangement that would support the recovery of fixed operating costs, but that the Province would not support an arrangement that would allow for the recovery of the carrying value of the station. As a result of this change in circumstance, OPG recorded the impairment loss. OPG has since negotiated a contract with the IESO, pursuant to the market rules, to recover its operating costs for a one-year period ending September 30, 2006. The contract with the IESO has been submitted to the OEB for approval.

OPG recorded an impairment loss of $63 million during 2005 relating to Units 2 and 3 of the Pickering A nuclear generating station, as a result of OPG's decision not to proceed with the return to service of these units. Upon consideration of the scope of the refurbishment work, the costs and the risks related to the return to service of these two units, and the Company's focus on improving the performance of its other nuclear units, OPG's Board of Directors decided that while technically feasible, the return to service of these units was not justified on a commercial basis. The impairment loss represented the carrying value, including construction in progress of these two units. In addition to the impairment loss for these two units, OPG recorded OM&A expenses of $57 million related to the write-off of inventory identified as excess or unusable, as a result of not returning Units 2 and 3 to service.

The Company also incurred higher nuclear maintenance and repairs in 2005 compared to 2004 related to continuing improvements in station reliability, and experienced an increase in pension and OPEB expenses primarily due to changes in economic assumptions.

Earnings in 2005 were also impacted by the effect of adopting rate regulated accounting for income taxes for the regulated segments of the business, and by changes in income tax positions. Effective April 1, 2005, OPG accounts for income taxes relating to the rate regulated segments of its business using the taxes payable method. Under this method, future income tax assets and liabilities associated with these segments are not recognized where those future income taxes are expected to be recovered in the regulated rates charged to customers in the future. As a result, during 2005, OPG did not record a future tax expense for the rate regulated segments of $157 million, which would have been recorded had OPG accounted for income taxes for the regulated segments using the liability method. As part of the transition, OPG also eliminated a net future income tax asset balance of $74 million relating to the rate regulated segments and recorded a corresponding one-time extraordinary loss.

During 2005, OPG recorded an income tax charge of $50 million to provide for a change in income tax liabilities related to certain income tax positions that the Company has taken in prior periods. OPG is responsible for making payments in lieu of corporate income and capital taxes to the Ontario Electricity Financial Corporation ("OEFC"). These payments are calculated in accordance with the *Income Tax Act* (Canada) and the *Corporations Tax Act* (Ontario), and are modified by the *Electricity Act, 1998* and related regulations.

In 2004, OPG's income tax expense was impacted by a reduction of $93 million in a valuation allowance for future income tax assets that had previously been established. This resulted in a reduction in the 2004 income tax provision, which did not recur in 2005.

Average Sales Prices

OPG's average sales prices by business segment, net of the revenue limit rebate for the period April 1, 2005 to December 31, 2005, and net of the Market Power Mitigation Agreement up to the inception of rate regulation on April 1, 2005 are as follows:

(¢/kWh)	**2005**	2004
Regulated – Nuclear[1]	**4.7**	4.1
Regulated – Hydroelectric[1]	**4.1**	4.1
Unregulated – Hydroelectric[2]	**5.2**	4.1
Unregulated – Fossil-fuelled[2]	**5.5**	4.2
OPG average price	**4.9**	4.1

1. During the period from April 1, 2005, electricity generation from stations in the Regulated – Nuclear segment received a fixed price of 4.95¢/kWh. During the same period, electricity generation 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.
2. During the period from April 1, 2005, 85 per cent of the electricity generation from unregulated stations, excluding the Lennox generating station and other contract volumes, was subject to a revenue limit based on an average price of 4.7¢/kWh.

OPG's average sales price was 4.9¢/kWh in 2005 compared to 4.1¢/kWh in 2004. OPG's average sales price was considerably less than the weighted average hourly Ontario electricity price of 7.2¢/kWh in 2005 as a result of regulated prices and the revenue limit rebate.

During 2005, OPG recorded $739 million related to the revenue limit rebate and $412 million related to the Market Power Mitigation Agreement rebate, compared to a Market Power Mitigation Agreement rebate of $1,154 million in 2004.

Electricity Generation

Electricity generated during 2005 from OPG's generating stations was 108.5 TWh compared to 105.0 TWh in 2004. The increase in generation was primarily a result of higher electricity demand and improved performance at OPG's fossil-fuelled and nuclear generating stations. The increase in generation was partly offset by a reduction in hydroelectric generation due to lower water levels.

OPG's results are impacted by changes in demand resulting from variations in seasonal weather conditions. The prolonged period of hot summer weather in 2005 resulted in a significant increase in the number of cooling degree days. The following table provides a comparison of heating and cooling degree days.

	2005	2004
Heating Degree Days[1]		
Total for year	**3,749**	3,751
Ten-year average	**3,704**	3,731
Cooling Degree Days[2]		
Total for year	**551**	233
Ten-year average	**356**	336

1. 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.
2. 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.

Cash Flow from Operations

Cash flow provided by operating activities during 2005 was $1,201 million compared to $226 million in 2004, an improvement of $975 million. The favourable change in cash flow was primarily due to higher revenue and earnings compared to 2004 and lower rebate payments in 2005. The revenue limit rebates totalling $739 million relating to 2005 are not required to be paid until 2006. The favourable changes were partly offset by higher pension contributions during 2005.

Pickering A Unit 1 Return to Service

Major construction for the return to service of Unit 1 at the Pickering A nuclear generating station commenced in July 2004. The construction phase of the project was completed in July 2005, with the removal of Unit 1 from the guaranteed shutdown state. On September 26, 2005, Unit 1 was synchronized to the provincial electricity grid, sending electricity from the unit to Ontario consumers for the first time since December 1997.

In November 2005, OPG declared the unit to be commercially available and informed the IESO that the unit was available for dispatch into the Ontario market, adding 515 MW of baseload capacity in Ontario. The project represented a complex construction challenge, encompassing more than 1.9 million hours of work and almost 3,000 people at its peak.

During the major construction phase of Unit 1 at the Pickering A nuclear generating station, the schedule and cost to complete the project was impacted by the discovery of feeder pipe thinning in areas not previously identified. This resulted in the need to perform additional inspections and the replacement of a feeder pipe, which was not included in the original scope of the project and the cost estimate. In addition, feeder issues resulted in the shutdown of Unit 4 at the Pickering A nuclear generating station. Resources were diverted from Unit 1 to address the Unit 4 feeder issue and to complete other outage work, which also contributed to the extension of the Unit 1 project schedule. The costs related to the feeder inspection and replacement program and the schedule extension were approximately $20 million.

Total cumulative expenditures for the return to service of Unit 1 at the Pickering A nuclear generating station to December 31, 2005 were $994 million, excluding the impact on costs of the feeder inspection and replacement, and the diversion of resources to Unit 4.

Recent Developments

Bruce Power

In October 2005, the Province and Bruce Power announced an agreement to refurbish the Bruce A nuclear generating station. Under the agreement, Bruce Power will refurbish and restart Units 1 and 2, refurbish Unit 3 when it reaches the end of its current operational life and replace the steam generators in Unit 4. The Bruce A units were taken out of service between 1995 and 1998 after a decision by the former Ontario Hydro.

In 2001, Bruce Power entered into a lease arrangement with OPG relating to the Bruce A and B nuclear generating stations, which are owned by OPG. Some of the terms of the 2001 lease were altered in 2003 when British Energy left the partnership due to insolvency. Under the terms of the 2003 lease, a return to service of any of the Bruce A units would result in an annual lease payment of $25.5 million per unit (in 2002 dollars, escalated at the Consumer Price Index ("CPI")). As part of the agreement reached in October 2005 between the Province and Bruce Power, OPG received a Shareholder Declaration from the Province instructing OPG's Board of Directors to accept certain amendments to the lease agreement. These amendments included a change to the provisions regarding the transfer of Bruce Power's interest in the site and included a reduction of the annual lease payment for three of the four refurbished Bruce A units to $5.5 million per unit (in 2002 dollars, escalated at CPI), after the planned future refurbishments are completed. These changes to the lease agreement will impact OPG when Units 1 and 2 of the Bruce A nuclear generating station are returned to service, and when Unit 3 is refurbished at the end of its current operational life. Other changes to the existing arrangements were made to address Cameco Corporation's decision not to participate in the refurbishment of the Bruce A nuclear generating station.

Nuclear Waste Management Organization Report
In November 2005, the Nuclear Waste Management Organization ("NWMO") submitted its report and recommendation on the long-term care of Canada's used nuclear fuel to the Minister of Natural Resources. The NWMO presented the following four options: deep geological disposal in the Canadian Shield, storage at nuclear reactor sites, long-term storage at a centralized storage facility, and an adaptive phased management approach. The NWMO recommended a phased management approach whose key attributes are: ultimate centralized containment and isolation of used nuclear fuel in an appropriate geological formation; phased and adaptive decision-making that is flexible in order to accommodate changes as they occur over time; optional shallow storage at the central site prior to placement in the repository; continuous monitoring; provision for retrievability; and citizen engagement. The federal government will decide which management alternative should be followed.

Ontario Power Authority Recommendations on Electricity Supply Sources in Ontario
In December 2005, the Ontario Power Authority ("OPA") provided its recommendations to the Minister of Energy on options for the future development of Ontario's electricity system to 2025. The recommendations take into account the Government's priorities of: creation of a conservation culture, preference for renewable sources of energy, and replacement of coal-fired generation for environmental and health reasons. The OPA consulted with a number of key stakeholders, including OPG.

The report indicates that conservation and new renewable sources will more than meet all of Ontario's growth in demand for electricity by 2025. This would not, however, replace the loss of capacity from the retirement of other supply sources. To replace the loss of capacity from the retirement of other supply sources, gas-fired generation should play a targeted, but critical role, and the share of nuclear generation in Ontario's supply mix should be maintained at its current level by refurbishing existing units, rebuilding on existing sites and undertaking "new build" plants. The OPA's recommendations would increase the share of renewable sources in Ontario's supply mix, maintain the share of nuclear generation, and replace coal by increasing the share of gas-fired generation and renewable resources. The Government is currently evaluating the report and assessing its recommendations.

Earnings Outlook

OPG's improved earnings outlook is forecast to continue in 2006 as a result of the implementation of the regulatory changes which took effect April 1, 2005, and continued improvements in generating station performance. Earnings from the regulated business will continue to reflect the introduction of regulated prices related to most of OPG's baseload hydroelectric and all of its nuclear facilities. Earnings from the unregulated business will reflect the revenue limits applied to a significant portion of the output from OPG's unregulated assets, which are higher than the limit previously prescribed by the Market Power Mitigation Agreement.

In addition, OPG's future earnings are forecast to be impacted by a number of factors including the closure of its coal-fired generating stations and the impact of the regulated prices established by the OEB.

Vision, Core Business and Strategy

OPG's mandate is to cost effectively produce electricity from its diversified generation assets, while operating in a safe, open and environmentally responsible manner. OPG and its sole Shareholder, the Province, reached agreement on this mandate during the third quarter of 2005. OPG's mandate is comprised of the following strategic objectives:

- OPG will operate its existing nuclear, hydroelectric and fossil generating assets as efficiently and cost effectively as possible, within federal and provincial legislative and regulatory frameworks, and in a manner that mitigates the Province's financial and operational risk.
- OPG's key nuclear objective will be the reduction of risk exposure to the Province arising from its investment in nuclear generating stations in general and, in particular, the refurbishment of older units, while continuing to operate with a high degree of vigilance with respect to nuclear safety.
- OPG will seek continuous improvement in its nuclear generation business and internal services as well as benchmark its performance in these areas against CANDU nuclear plants world-wide and the top quartile of private and publicly-owned nuclear electricity generators in North America. OPG's top operational priority will be to improve the operation of its existing nuclear fleet.
- OPG will continue to operate its fossil fleet, including coal plants, according to normal commercial principles taking into account the Government's coal replacement policy and recognizing the role that fossil-fuelled plants play in the Ontario electricity market.
- With respect to investment in new generation capacity, OPG's priority will be hydroelectric capacity. OPG will seek to expand, develop, and/or improve its hydroelectric generation capacity through expansion and redevelopment of its existing sites as well as the pursuit of new projects where feasible. OPG will undertake these investments through partnerships or on its own, as appropriate.
- OPG will operate in accordance with the highest corporate standards, including but not limited to the areas of corporate governance, social responsibility, corporate citizenship and environmental stewardship, taking into account the Government's coal replacement policy.

To accomplish its mandate and strategic objectives, OPG is focusing on the following four strategies: improving generating asset performance through production efficiencies and increased reliability; increasing its generating capacity; achieving excellence in corporate governance, safety, social responsibility, corporate citizenship and environmental stewardship; and effectively managing its costs.

Improving the Performance of Generating Assets

Nuclear Generating Assets

OPG's strategic objective is to operate the Darlington and Pickering A and B stations in a safe, efficient and cost effective manner, while undertaking prudent investments to improve their reliability and predictability. To achieve this objective, programs and initiatives have been implemented that will: continue to improve safety performance, reduce forced outages through improvements in equipment reliability, optimize planned outages, reduce maintenance backlogs, mitigate technological risks through comprehensive inspection and testing programs, focus on production unit energy costs, and address resource planning issues.

In August 2005, OPG decided to devote its resources and expertise to maximizing the performance of its ten existing nuclear units, rather than refurbish Units 2 and 3 at the Pickering A nuclear station. As a result, OPG has initiated the process of placing Pickering Units 2 and 3 in safe storage.

Hydroelectric Generating Assets

OPG's strategic objective is to optimize production from its existing hydroelectric generating assets. To continue to optimize production, programs are in place to: replace aging equipment, automate obsolete control equipment, accelerate runner upgrades, and improve availability through enhanced maintenance practices. These programs will result in increased capacity, extended service lives, and lower long-term operating and maintenance costs.

Fossil-Fuelled Generating Assets

OPG's strategic objective, taking into account the Government's coal replacement policy, is to maintain the productive capability of its coal-fired facilities, while continuing to operate them in an environmentally responsible manner. To achieve this objective, programs and initiatives are in place to: address the impacts of increased unit starts and stops, in part due to the role that the fossil-fuelled plants perform as intermediate and peaking facilities, ensure continued environmental compliance, and retain competent staff to continue to operate the units until their closure.

In October 2005, OPG received a Shareholder Declaration from the Province instructing OPG's Board of Directors to convert the Thunder Bay generating station to run on natural gas. Under the declaration, the Province will put in place appropriate cost recovery mechanisms covering initial capital and development expenditures, ongoing operating costs and an appropriate return to OPG. The cost recovery mechanisms are required to ensure that OPG is able to record the conversion costs as an asset. The project is expected to be complete by December 2007.

Increasing OPG's Generating Capacity

OPG's strategy with respect to increasing its generating capacity is to expand, develop, and/or improve its hydroelectric generation capacity through expansion and redevelopment of its existing sites, as well as the pursuit of new projects where feasible. OPG will undertake these investments on its own or through partnerships.

Niagara Tunnel

In June 2004, OPG announced and the Government endorsed the decision to proceed with a new water diversion tunnel that will increase the amount of water flowing to existing turbines at the Sir Adam Beck generating stations in Niagara. This tunnel will allow the Beck generating facilities to utilize available water more effectively, and is expected to increase annual generation on average by about 1.6 TWh. OPG undertook an open, competitive and international process to select the successful contractor, with three pre-qualified companies submitting detailed design-build proposals in May 2005. Following approval by OPG's Board of Directors and cabinet approval to finance the project through the OEFC, OPG awarded a contract to Strabag AG in August 2005 to design and construct the 10.4 kilometre tunnel and associated facilities. The value of the design-build contract is approximately $600 million, with the total project expected to cost approximately $985 million.

Site preparation work started in September 2005. Blasting for the outlet canal started in December 2005 and is expected to continue through April 2006. Project completion is expected by late 2009. The project is currently on schedule and within the expected cost, with expenditures through December 2005 totalling $82 million.

Lac Seul

In December 2005, the OPG Board of Directors approved a $47 million project to construct a new 12.5 MW hydroelectric generating station on the English River, just east of OPG's existing Ear Falls generating station, which is 370 kilometres northwest of Thunder Bay, Ontario. The new Lac Seul generating station will utilize a majority of the spill currently passing the existing Ear Falls generating station, thus increasing the overall efficiency, capacity and energy generated from this location. A design-build contract was awarded to SNC Lavalin Power Ontario Inc. Construction commenced in January 2006, with the in-service date planned for the fourth quarter of 2007. As at December 31, 2005, approximately $3 million has been spent, which includes engineering, environmental approvals and geotechnical analysis.

Other Hydroelectric Projects

In addition to the Niagara tunnel and Lac Seul hydroelectric projects, OPG is exploring the feasibility of developing a number of potential hydroelectric projects in Northern Ontario.

Pickering A Unit 1 Return to Service

In November 2005, OPG declared Unit 1 at the Pickering A nuclear generating station to be commercially available and informed the IESO that the unit was available for dispatch into the Ontario market, adding 515 MW of baseload capacity in Ontario.

Portlands Energy Centre

OPG entered into a partnership with TransCanada Energy Ltd. ("TransCanada"), called Portlands Energy Centre L.P. ("PEC"), to pursue the development of a 550 MW gas-fired, combined cycle station on the site of the former R.L. Hearn generating station, near downtown Toronto. The generating station would help to meet the growing energy needs of Toronto's downtown core. The IESO identified, in its December 2005 18-month outlook, that Toronto faces rotating blackouts within the next two years unless urgent action is taken to install new power generation.

The Ministry of Energy has indicated that it will issue a separate directive to the OPA to procure up to 600 MW of generation for downtown Toronto. PEC intends to participate in this procurement process.

Excellence in Corporate Governance, Safety, Social Responsibility, Corporate Citizenship and Environmental Stewardship

Another of OPG's strategic objectives is to operate in accordance with the highest corporate standards, including, but not limited to the areas of corporate governance, safety, and sustainable development, taking into account the Government's coal replacement policy.

Corporate Governance

OPG's Board of Directors is made up of individuals with substantial expertise in managing and restructuring large businesses, managing and operating nuclear stations, managing capital intensive companies, and overseeing regulatory, government and public relations. The Board has established a number of committees to focus on areas critical to the success of the Company.

OPG's corporate governance approach is to continually improve the policies and procedures used to direct and manage the corporation to enhance Shareholder value and ensure financial viability. OPG continues to implement initiatives to enhance corporate governance practices in line with existing Ontario Securities Commission ("OSC") regulatory requirements, with the objective of strengthening the organization. These initiatives are described in the Corporate Governance section on pages 50 to 53.

Safety

OPG is committed to achieving excellent safety performance, striving for continuous improvement with the goal of minimizing injuries. A primary objective is to achieve excellence in employee and public safety through the development and implementation of formal safety management systems, targeted risk mitigation programs, and a corporate commitment to safety. Continuous oversight and reporting provide management with information on the effectiveness of the safety management efforts, compliance with legal and corporate requirements, and safety performance trends. Oversight activities include internal and external safety management system audits, work protection code audits, and specific operational safety risk reviews. OPG also has a rigorous incident management system, which requires that all incidents, including near misses, be reported and investigated, and that corrective action plans are developed to prevent reoccurrences.

A contractor management program has been implemented to ensure that contractors contribute to our strong safety culture and maintain a level of safety equivalent to that of OPG employees. Initiatives are in place to address young worker safety issues within OPG and in the communities where we operate. A commitment to public safety is an important part in the operation of our generating stations, including standards established in the area of public waterways safety.

In 2005, OPG was the first and only recipient of the Electrical and Utilities Safety Association ("E&USA") Gold Award in recognition for effective safety management systems and a strong safety culture across the Company. This recognition followed a detailed assessment by the E&USA of OPG's safety management systems and interviews with staff from across the Company.

OPG measures its safety performance primarily through two performance indicators – Accident Severity Rate ("ASR") and All Injury Rate ("AIR"). The ASR is a measure of the number of days lost due to injuries. In 2005, OPG experienced 2.03 days lost per 200,000 hours worked. The AIR provides a measure of the frequency of injuries resulting in lost time or requiring medical treatment. In 2005, OPG experienced 1.33 injuries per 200,000 hours worked. OPG's ASR and AIR continue to be within the top quartile (2002 to 2004 average) of the Canadian Electricity Association.

Sustainable Development

OPG's sustainable development policy states that OPG will apply the principles of sustainable development to the generation and sale of electricity. OPG is committed to minimizing our impact on the environment; operating our facilities safely, reliably and responsibly; and being an engaged and productive member of our host communities. OPG's sustainable development activities can be divided into two categories: Environmental Stewardship and Social and Corporate Responsibility.

Environmental Stewardship

OPG's Sustainable Development Policy commits OPG to meet all applicable legislative requirements and voluntary environmental commitments. Other goals include integrating environmental factors into business planning and decision-making, applying the precautionary principle in assessing risks to human health and the environment, and maintaining environmental management systems ("EMSs") at our generating facilities consistent with the ISO 14001 standard. More information on OPG's emissions into the environment and compliance with environmental laws is included within the Risk Management – Environmental Risk section.

OPG utilizes a number of performance indicators to monitor environmental performance, including sulphur dioxide ("SO_2") and nitrogen oxides ("NO_X"). Acid gas (SO_2 and NO_X) emissions were 139 Gigagrams (Gg) in 2005 compared to 143 Gg in 2004. The reduction in emissions was primarily a result of improved performance from the selective catalytic reduction equipment installed at OPG's Nanticoke and Lambton fossil-fuelled generation stations and the use of lower sulphur fuels at OPG's fossil-fuelled stations, even though fossil-fuelled generation volumes were higher in 2005.

Social and Corporate Responsibility

Enhancing the quality of life in communities where companies operate is a corporate responsibility as well as a societal expectation. OPG is committed to being an active and good corporate citizen by strengthening relationships with the communities that OPG serves and those that host OPG's generating facilities. At the corporate level, as well as through the actions of employees, OPG plays a significant role in local communities by donating time and resources. The Corporate Citizenship Program provides financial and in-kind support to registered charities and not-for-profit environmental, educational and community organizations whose initiatives reflect OPG's values. Employees donate funds through an annual charity campaign and their time, expertise and energy through numerous personal acts of volunteerism.

Effective Cost Management

OPG's strategic objectives include operating its generating assets as cost effectively as possible, including the corporate and business unit support provided to those generating assets. OPG has commenced various initiatives aimed at better identifying and managing costs over and above those strategies aimed at improving generating asset performance. These initiatives include: an activity-based costing review of activities and processes in nuclear; benchmarking against industry-wide standards; a comprehensive review of project management intended to better integrate project planning, estimation, tracking of costs and schedule processes; ongoing review of opportunities for efficient fuel procurement, particularly relating to the fossil-fuelled generating stations; alignment of generating assets into technology-based businesses and full cost allocation review to improve management of these facilities; changes to vendor payment terms to improve cash flow; consolidation of functions supporting the restructured energy markets business; and key improvement initiatives aimed at streamlining information technology services and managing associated costs.

Capability to Deliver Results

Capital Resources and Liquidity

OPG's financial condition has improved following implementation of the regulatory changes which were introduced in 2005. In addition, in 2005, OPG secured dedicated financing for the Niagara tunnel and Thunder Bay generating station projects and additional long-term financial support from its Shareholder, the Province, in the form of long-term debt, on commercial terms and rates.

External financing consists primarily of a bank syndicated credit facility under which OPG issues commercial paper to fund its short-term requirements, and a number of financing arrangements held with OPG's Shareholder. OPG has the necessary working capital and financing resources to meet its obligations and commitments in 2006. OPG's liquidity is constrained by the revenue limit rebates on OPG's unregulated operations, which the Government recently announced would be extended for a period of three years.

Generating Assets

OPG continues to focus on maintaining and improving the performance of its generating stations.

OPG has increased the productive capacity of its hydroelectric stations, extended their service lives and lowered OM&A expenses through significant capital investment for the replacement of aging equipment, upgrades to runners and station automation, and enhanced maintenance practices. Programs are in place to further improve the hydroelectric stations, which already operate with high efficiency and reliability.

OPG is implementing initiatives that will improve the reliability and predictability of each of the nuclear generating stations. These initiatives are designed to address the specific technology requirements and risks at each of OPG's nuclear generating stations. The Darlington nuclear generating station is the most recently constructed station in OPG's nuclear fleet and operates with the highest reliability. The two operating units at the Pickering A nuclear station have recently been refurbished and are in good material condition. Programs are underway at the Pickering B nuclear generating station to mitigate technological risks and to improve its condition and performance. The performance of the Pickering B nuclear station has improved in 2005 compared to its performance in recent years.

OPG will continue to maintain the reliability and productive capacity of its coal-fired generating stations until their scheduled closure dates.

OPG has a number of potential sites for new generating asset development in Ontario. The completion of the decommissioning activity at OPG's Lakeview generating station will provide a brownfield site with the potential for development of additional generating capacity in the Greater Toronto Area.

Skilled Workforce

As of December 31, 2005, OPG had approximately 11,300 full-time employees. OPG has considerable experience in operating and maintaining generating stations through its trained and qualified technical employees. Due to an aging workforce, OPG's challenge is to attract and retain a skilled workforce to replace retiring employees. Approximately 34 per cent of the workforce was over the age of 50 at December 31, 2005. OPG has initiated a comprehensive resource and succession planning program to address issues related to the high percentage of employees eligible for retirement over the next five years, as well as those issues associated with the closure of the coal-fired generating stations.

The Company recently reached tentative agreements with the Power Workers Union, which are subject to membership ratification. The Company also recently renewed its labour agreement with the Society of Energy Professionals, extending the agreement to December 31, 2010. As of December 31, 2005, the Company had approximately 90 per cent of its regular labour forces covered by collective bargaining agreements.

Ontario Electricity Market Trends

In 2005, the Government implemented electricity sector reforms, which included electricity prices that better reflect the true cost of electricity and the termination of a financially unsustainable rebate. Effective April 1, 2005, the output from OPG's baseload hydroelectric and nuclear facilities became rate regulated, while output from its remaining hydroelectric facilities and its fossil-fuelled and wind generating stations remain unregulated. However, the majority of the generation output from these unregulated facilities is subject to a revenue limit.

Electricity demand is primarily impacted by weather and economic activity. Ontario's IESO reported that it faced a number of challenges maintaining the reliability of Ontario's bulk power system during the summer of 2005. Soaring temperatures brought significant demand and drought-like conditions limited hydroelectric generation, resulting in a continued strain on the power system. The IESO relied on extensive use of emergency control actions, including public appeals to reduce consumption, and voltage reductions. This occurred despite good performance and availability of Ontario generation and transmission facilities and the support from neighbouring markets. Ontario's peak electricity demand in 2005 of 26,160 MW represented an increase of 4.7 per cent over that of 2004. The expected peak demand in the summer of 2006, under normal weather conditions, is forecast by the IESO to be 25,917 MW. By 2015, Ontario's electricity peak demand, under normal weather conditions, is forecast to reach 26,900 MW and under extreme weather conditions, is forecast to approach 30,000 MW.

With respect to electricity supply, the IESO reported that increased supply brought into service in the fourth quarter of 2005 (515 MW from Unit 1 at the Pickering A nuclear generating station) and planned market enhancements in the first half of 2006 contribute to a more positive outlook for Ontario's overall supply adequacy picture over the next 18 months. The overall outlook for resource availability continues to indicate that for most weeks during this time frame, there are sufficient resources to meet demand, under the normal weather demand scenario. Under extreme weather conditions, the outlook identifies significant reliance on imports in many weeks, to meet demand. While the overall supply situation appears adequate, concerns remain in a number of areas within Ontario, particularly in the Greater Toronto Area, where the need for new supply and transmission facilities is particularly urgent.

In February, the IESO released its report titled, "The Ontario Reliability Outlook". The Outlook highlights the complexity of the changes and major infrastructure projects necessary to implement the Government's off-coal strategy. The IESO advised of the need for close coordination and continuous monitoring of progress and system impacts to maintain system reliability. The Outlook talks of the need for prudence in ensuring that Lambton and Nanticoke units are capable of operating beyond the currently specified dates for closure. OPG is committed to ensuring that its plants remain in as good operating condition as they are today, until the date the Company is required to close them by its Shareholder.

At the end of 2005, Ontario's existing installed generating capacity was 30,631 MW, a decrease of 533 MW over that of the previous year. This decrease was caused by the closure of OPG's Lakeview generating station, partially offset by the return to service of Unit 1 at OPG's Pickering A nuclear generating station. OPG's in-service capacity at the end of 2005 of 22,173 MW represented 72 per cent of Ontario's capacity. The IESO estimates that by 2015, approximately 12,850 MW of Ontario's electricity requirements will have to be met with new supply, refurbished generation or conservation measures. This estimate is consistent with that provided by the OPA in its report to the Minister of Energy on options for the future development of Ontario's electricity system to 2025.

In 2005, energy consumed in Ontario of 157.0 TWh represented an increase of 2.3 per cent over 2004 consumption. OPG's generating facilities produced 69 per cent of this amount. The IESO forecast for energy consumption in 2006 is 157.0 TWh.

Electricity prices typically peak when demand is at its highest, since high marginal cost peaking generating stations are required to meet that demand. Electricity prices also exhibit seasonal variations related to changes in demand. Ontario's weighted average hourly electricity price in 2005 of 7.2¢/kWh was significantly higher than in 2004. Changes in electricity prices have a significant impact on OPG's financial performance. This impact is significantly lessened by the application of fixed electricity prices for the output of assets subject to rate regulation and the effect of the revenue limit.

Fuel prices can have a significant impact on revenue and operating profits, both in terms of the underlying commodity price and the United States ("U.S.")/Canadian dollar exchange rate. During 2005, there were marked increases in the spot price for Appalachian and Powder River Basin coal, uranium, natural gas and oil, all of which are used to meet OPG's fuel requirements. OPG has a fuel hedging program that includes fixed price contracts for fossil and nuclear fuels. Foreign exchange derivatives are used to hedge exposure to anticipated U.S. dollar denominated purchases. As a result of volatile world energy markets, OPG expects this trend of increasing commodity prices to continue.

Business Segments

Prior to the introduction of rate regulation, OPG had two reportable business segments: Generation and Energy Marketing. A separate category, Non-Energy and Other, included revenue and certain costs not allocated to its business segments. With the introduction of rate regulation, OPG changed the definition of business segments with effect from April 1, 2005 in recognition of the different economic characteristics of the Company's operations. The business segments are: Regulated – Nuclear, Regulated – Hydroelectric, and Unregulated Generation. In addition, OPG continues to report a separate category, Other, which includes trading activities that previously comprised the Energy Marketing business segment, and revenues and certain costs neither attributable nor allocated to its business segments.

OPG has entered into various energy and related sales contracts with its customers to hedge commodity price exposure to changes in electricity prices associated with the spot market for electricity in Ontario. Contracts that are designated as hedges of OPG's generation revenues are included with electricity production revenues in each segment up to March 31, 2005, and in the Unregulated Generation segment after that date. Gains or losses on these hedging transactions are recognized in revenue over the term of the contract when the underlying transaction occurs.

Regulated – Nuclear Segment

OPG's Regulated – Nuclear business segment operates in Ontario, generating and selling electricity from the nuclear generating stations that it owns and operates. The business segment includes electricity generated by the Pickering A and B, and Darlington nuclear generating stations.

OPG's Regulated – Nuclear business segment includes revenue under the terms of a lease arrangement with Bruce Power related to the Bruce nuclear generating stations. The arrangement includes lease revenue, interest income and revenue from engineering analysis and design, technical and other services. The Regulated – Nuclear business segment also includes revenue earned from isotope sales and ancillary services. Ancillary revenues are earned through voltage control/reactive support. These earnings are included in the Regulated – Nuclear business segment since they were included in determining the regulated price for production from the nuclear facilities.

Regulated – Hydroelectric Segment

OPG's Regulated – Hydroelectric business segment operates in Ontario, generating and selling electricity from its baseload hydroelectric generating stations. The business segment includes electricity generated by the Sir Adam Beck 1, 2 and Pump generating station, DeCew Falls 1 and 2, and the R.H. Saunders hydroelectric facilities. The Regulated – Hydroelectric business segment also includes ancillary revenues related to these stations earned through offering available generating capacity as operating reserve and through the supply of other ancillary services including voltage control/reactive support, certified black start facilities and automatic generation control.

Unregulated Generation Segment

OPG's Unregulated Generation business segment operates in Ontario, generating and selling electricity from its fossil-fuelled generating stations and from the hydroelectric generating stations not included in the Regulated – Hydroelectric segment. The Unregulated Generation business segment also includes ancillary revenues earned through offering available generating capacity as operating reserve, and through the supply of other ancillary services including voltage control/reactive support, certified black start facilities and automatic generation control, and revenues from other services.

Other

OPG earns revenue from its joint venture share of the Brighton Beach Power Limited Partnership ("Brighton Beach") related to an energy conversion agreement between Brighton Beach and Coral Energy Canada Inc. ("Coral"). In addition, the Other category includes revenue from real estate rentals.

The revenue and expenses related to OPG's trading and other non-hedging activities are also included in the Other category. As part of these activities, OPG transacts with counterparties in Ontario and neighbouring energy markets in predominantly short-term trading activities of typically one year or less in duration. These activities relate primarily to physical energy that is purchased and sold at the Ontario border, sales of financial risk management products and sales of energy-related products. All contracts that are not designated as hedges are recorded as assets or liabilities at fair value, with changes in fair value recorded in other revenue as gains or losses.

Key Generation and Financial Performance Indicators

To accurately reflect the measures that are critical to successful implementation of its strategy and achievement of its goals, OPG has expanded its disclosure of key performance indicators. These indicators are defined in this section and are discussed in both the Vision, Core Business and Strategy, and Discussion of Operating Results sections. Key performance indicators that directly pertain to OPG's mandate and corporate strategies are measures of production efficiency, cost effectiveness, safety and environmental performance.

Nuclear Unit Capability Factor

OPG's nuclear stations operate as baseload facilities as they have low marginal costs and are not designed for fluctuating production levels to meet peaking demand. The nuclear unit capability factor is a key measure of nuclear station performance. It is the amount of energy that the unit(s) generated over a period of time, adjusted for external energy losses such as transmission or demand limitations, as a percentage of the amount of energy that would have been produced over the same period had the unit(s) produced maximum generation. Capability factors are primarily impacted by planned and unplanned outages.

Fossil-fuelled and Hydroelectric Equivalent Forced Outage Rate ("EFOR")

OPG's fossil-fuelled stations provide a flexible source of energy and operate as baseload, intermediate and peaking facilities, depending on the characteristics of the particular stations. OPG's hydroelectric stations operate primarily as baseload facilities and provide a reliable and low-cost source of renewable energy. A key measure of the reliability of the fossil-fuelled and hydroelectric stations is their ability to be available to produce electricity when called upon. EFOR is an index of the reliability of the generating unit measured by the ratio of time a generating unit is forced out of service, including any forced deratings, compared to the amount of time the generating unit was available to operate.

Nuclear Production Unit Energy Cost ("PUEC")

Nuclear PUEC is used to measure the cost effectiveness of OPG's nuclear generating assets. It is a measure of the cost of producing a unit of electricity. Nuclear PUEC is defined as nuclear fuel, OM&A expenses including allocated corporate costs, and variable costs related to used fuel disposal and the disposal of other low and intermediate level radioactive waste materials, divided by total energy produced.

Fossil-fuelled OM&A expense per MW

Since fossil-fuelled generating stations are primarily employed during periods of intermediate and peak demand, the cost effectiveness of these stations is measured by their total OM&A expenses, including allocated corporate costs, divided by total station nameplate capacity.

Hydroelectric OM&A expense per MWh

Hydroelectric OM&A expense per MWh is used to measure the cost effectiveness of the hydroelectric generating stations. It is defined as total hydroelectric OM&A expenses, including allocated corporate costs, divided by hydroelectric electricity generation.

Other Key Indicators

In addition to performance and cost effectiveness indicators, OPG has identified various social and environmental indicators. These indicators are discussed in the section titled Vision, Core Business and Strategy – Excellence in Corporate Governance, Safety, Social Responsibility, Corporate Citizenship and Environmental Stewardship.

Discussion of Operating Results by Business Segment

This section summarizes OPG's key results by segment for the years ended December 31, 2005 and 2004. Although the regulations pursuant to the *Electricity Restructuring Act, 2004* became effective commencing April 1, 2005, results for the quarters prior to April 1, 2005 have been reclassified according to the new business segment definitions. The prior period results from OPG's nuclear and hydroelectric generating stations that are now regulated have been reclassified into the Regulated – Nuclear and Regulated – Hydroelectric segments for comparative purposes. Similarly, results from OPG's unregulated generating stations have been reclassified into the Unregulated Generation segment. Accordingly, revenues reflect spot market prices received for electricity sales net of the Market Power Mitigation Agreement rebate up to the inception of rate regulation on April 1, 2005.

The operating results for the period prior to rate regulation reflect a significantly different economic environment from that introduced by rate regulation.

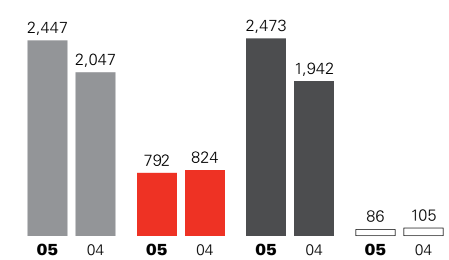
The following table provides a summary of revenue, earnings and operating statistics by business segment:

(millions of dollars)	**2005**	2004
Revenue, net of Market Power Mitigation Agreement rebate and revenue limit rebate		
Regulated – Nuclear	**2,447**	2,047
Regulated – Hydroelectric	**792**	824
Unregulated Generation	**2,473**	1,942
Other	**86**	105
	5,798	4,918
Income (loss) before interest, income taxes and extraordinary item		
Regulated – Nuclear	**(10)**	(468)
Regulated – Hydroelectric	**375**	406
Unregulated Generation	**406**	212
Other	**(16)**	1
	755	151
Electricity Generation[1] (TWh)		
Regulated – Nuclear	**45.0**	42.3
Regulated – Hydroelectric	**18.5**	18.9
Unregulated Generation – Hydroelectric	**14.1**	16.8
Unregulated Generation – Fossil-fuelled	**30.9**	27.0
Total electricity generation	**108.5**	105.0
Nuclear unit capability factor[2] (per cent)		
Darlington	**90.6**	88.2
Pickering A	**69.9**	75.7
Pickering B	**77.7**	69.8
Equivalent forced outage rate (per cent)		
Regulated – Hydroelectric	**1.2**	2.2
Unregulated Generation – Hydroelectric	**1.4**	1.4
Unregulated Generation – Fossil-fuelled	**15.9**	18.7
Nuclear PUEC ($/MWh)	**39.70**	39.20
Regulated – Hydroelectric OM&A expense per MWh ($/MWh)	**4.17**	3.92
Unregulated – Hydroelectric OM&A expense per MWh ($/MWh)	**10.38**	7.68
Unregulated – Fossil-fuelled OM&A expense per MW ($000/MW)	**52.2**	46.0

1. Electricity generation is presented in accordance with OPG's business segments, with the exception of the Unregulated Generation segment, for which generation from hydroelectric and fossil-fuelled generating stations is shown separately.
2. Capability factors by industry definition exclude grid-related unavailability.

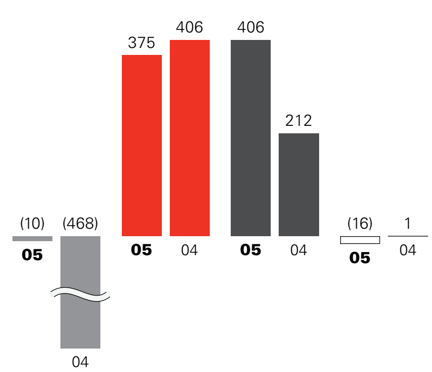
Revenue, Net of Market Power Mitigation Agreement Rebate and Revenue Limit Rebate
(millions of dollars)

Regulated – Nuclear
Regulated – Hydroelectric
Unregulated Generation
Other

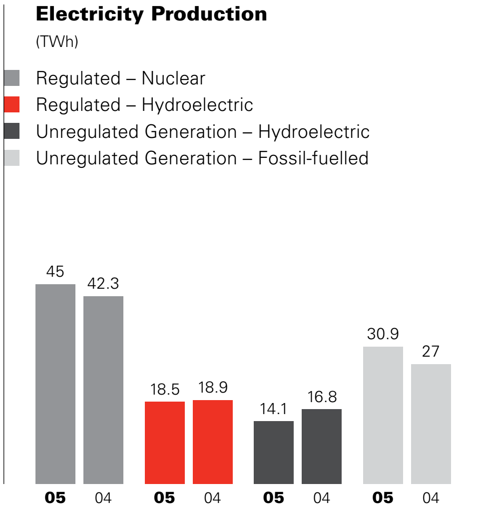


Income (loss) Before Interest, Income Taxes and Extraordinary Item
(millions of dollars)

Regulated – Nuclear[1]
Regulated – Hydroelectric
Unregulated Generation[2]
Other



1. The Regulated – Nuclear segment includes the asset impairment loss of $63 million and inventory write-off of $57 million related to the Pickering A Nuclear generating station Units 2 and 3 in 2005.
2. Unregulated Generation segment includes the impairment loss of $202 million related to the Lennox generating station in 2005.



Regulated – Nuclear Segment

(millions of dollars)	2005	2004
Revenue, net of Market Power Mitigation Agreement rebate	**2,447**	2,047
Fuel expense	**115**	108
Gross margin	**2,332**	1,939
Operations, maintenance and administration		
Expenses excluding Pickering A return to service	**1,784**	1,611
Pickering A return to service	**4**	271
Depreciation and amortization	**374**	360
Accretion on fixed asset removal and nuclear waste management liabilities	**467**	445
Earnings on nuclear fixed asset removal and nuclear waste management funds	**(381)**	(313)
Property and capital taxes	**31**	33
Income (loss) before the following:	**53**	(468)
Impairment loss	**63**	–
Loss before interest, income taxes and extraordinary item	**(10)**	(468)

Revenue

(millions of dollars)	2005	2004
Spot market sales, net of hedging instruments	**662**	2,090
Market Power Mitigation Agreement rebate	**(160)**	(374)
Regulated generation sales	**1,621**	–
Variance accounts	**(1)**	–
Other	**325**	331
Total revenue	**2,447**	2,047

Regulated – Nuclear revenue was $2,447 million for the year ended December 31, 2005 compared to $2,047 million in 2004. The increase in revenue was primarily due to higher sales prices related to the introduction of regulated rates effective April 1, 2005, which exceeded OPG's average spot market price net of the Market Power Mitigation Agreement rebate in 2004. Revenue also increased as a result of higher electricity generation of 2.7 TWh during 2005 compared to the prior year.

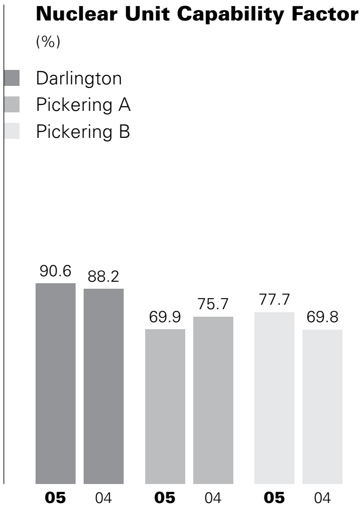
Electricity Prices

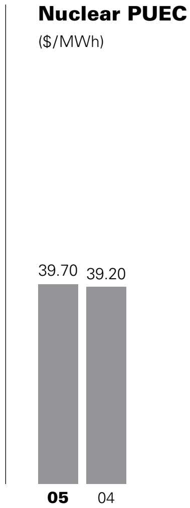
Since market opening on May 1, 2002, and prior to April 1, 2005, OPG was required under its generation licence issued by the OEB to comply with prescribed market power mitigation measures, including a rebate mechanism. Under the Market Power Mitigation Agreement, OPG had been required to pay a rebate to the IESO equal to the excess, if any, of the average hourly spot energy price over 3.8¢/kWh for the amount of energy sales subject to the rebate mechanism for those generating stations that OPG continued to control. The IESO passed the rebate on to consumers. The amount of energy generated by OPG that was subject to the rebate mechanism was approximately 80.0 TWh on an annual basis.

Electricity generation from stations in the Regulated – Nuclear segment received a fixed price of 4.95¢/kWh since April 1, 2005. OPG's average sales price for the year ended December 31, 2005 was 4.7¢/kWh, after taking into account the regulated rate received from April 1, 2005 to December 31, 2005, and OPG's average spot market sales price, net of the Market Power Mitigation Agreement rebate for the first quarter of 2005. In 2004, OPG's average sales price after taking into account the Market Power Mitigation Agreement rebate was 4.1¢/kWh.

Volume

Total nuclear generation for the year ended December 31, 2005 increased to 45.0 TWh from 42.3 TWh in 2004. The increase in volume was primarily due to improved performance at the Pickering B and Darlington nuclear generating stations compared to 2004. Both stations experienced fewer unplanned outage days, and there were fewer planned outage days at the Pickering B generating station. The impact on volume from the return to service of Unit 1 at the Pickering A nuclear generating station in 2005, was largely offset by the impact of higher outage days for Unit 4 in 2005, primarily related to the shutdown of Unit 4 in April 2005 for inspection of feeder pipes. Unit 4 was returned to service in July 2005, after two feeder pipes were replaced.





The Darlington nuclear generating station's unit capability factor for 2005 of 90.6 per cent reflected continued strong performance. The reduction in outage days at the Pickering B nuclear generating station resulted in a significant improvement in its unit capability factor in 2005 to 77.7 per cent compared to 69.8 per cent in 2004. The unit capability factor for the Pickering A nuclear generating station decreased to 69.9 per cent in 2005 from 75.7 per cent in 2004, as a result of the Unit 4 outage for inspection and replacement of feeder pipes.

Fuel Expense

Fuel expense for the year ended December 31, 2005 was $115 million compared to $108 million in 2004. Fuel expense for the nuclear generating stations was only marginally impacted by the changes in generation volumes in 2005 compared to 2004 due to the low marginal cost nature of nuclear generation.

Operations, Maintenance and Administration

OM&A expenses, excluding those related to the Pickering A return to service initiative, were $1,784 million for the year ended December 31, 2005 compared to $1,611 million in 2004, an increase of $173 million. As part of OPG's objective to improve the performance of its nuclear generating stations, the Company has committed additional resources in an effort to maximize the operating availability and reliability of these stations. OM&A expenses for nuclear maintenance and repairs increased by $101 million compared to 2004. These expenditures related to ongoing maintenance costs to address plant condition, regulatory requirements, and improvement projects. OM&A expenses also increased in 2005 compared to 2004 due to the write-off of $57 million of excess inventory as a result of the decision not to return Pickering A generating station Units 2 and 3 to service.

In addition, pension and OPEB costs increased by $36 million compared to 2004, primarily the result of changes in economic assumptions related to discount rates. The impact of these increases in expense was partly offset by reductions in other costs.

Nuclear PUEC in 2005 increased to $39.70/MWh compared to $39.20/MWh in 2004 primarily as a result of the additional expenditures on maintenance and repairs, and the increase in pension and OPEB costs.

Pickering A Return to Service

Effective January 1, 2005, in accordance with a regulation pursuant to the *Electricity Restructuring Act, 2004,* OPG established a balance sheet deferral account for non-capital costs associated with the return to service of Pickering A nuclear generating station units. These deferred costs will be charged to operations in subsequent periods in accordance with the terms of the above referenced regulation. The regulation requires the OEB to ensure recovery of any balance recorded in the deferral account over a period not exceeding 15 years. This approach is consistent with one of the objectives of rate regulation, which is to ensure that present customers are not burdened with costs incurred for the benefit of future customers, and with generally accepted accounting principles in that the financial effects of regulation can lead to the recording of assets and liabilities that would not otherwise be recognized by a non-rate-regulated entity. Amortization of this deferral account began during the fourth quarter of 2005 on the date of the return to commercial service of Unit 1 of the Pickering A nuclear generating station. The amortization of $4 million was charged to OM&A expense.

As a result of the regulation, non-capital costs related to the Pickering A return to service initiative were excluded from OM&A during 2005, with the exception of that portion amortized in 2005 due to the return to service of the Pickering A generating station Unit 1. Had these expenditures not been deferred, OM&A expense of $258 million would have been recognized in 2005 compared to $271 million last year.

Impairment of Long-Lived Assets – Pickering A Generating Station Units 2 and 3

As a result of the decision not to proceed with the return to service of Pickering nuclear generating station Units 2 and 3, the Company recorded an impairment loss of $63 million in the second quarter of 2005 related to the carrying amount of these two units, including construction in progress. OPG continues to assess the need to provide for additional charges as a result of the decision not to proceed with the return to service of Units 2 and 3, including the cost associated with preparing the units for safe storage, the impact on cost estimates for asset retirement obligations, and any other exit costs. OPG completed a preliminary assessment of additional charges during the fourth quarter of 2005.

Depreciation and Amortization

Depreciation and amortization expense for the year ended December 31, 2005 was $374 million compared to $360 million in 2004. The increase was primarily due to fixed asset additions at the Pickering B and Darlington nuclear generating stations. In addition, the return to commercial service of Unit 1 at the Pickering A nuclear generating station in November 2005 resulted in an increase in depreciation expense of $4 million in 2005, and will initially add approximately $21 million to annual depreciation expense thereafter. These increases were partially offset by an extension of the remaining service life of Unit 4 at the Pickering A nuclear generating station. During the fourth quarter, as a result of the return to commercial service of the Pickering A generating station Unit 1, OPG extended, for purposes of calculating depreciation, the remaining service life of the Pickering A generating station Unit 4 to 2021, consistent with the expected service life of Unit 1. This reduces depreciation expense by approximately $16 million annually over the period to 2017, excluding the impact of future asset additions. OPG is in the process of reviewing the remaining service lives of its other nuclear generating stations.

Accretion

OPG records the present value of its future costs for fixed asset removal and nuclear waste management as a long-term liability. This liability is discussed in Note 9 to the consolidated financial statements as at and for the year ended December 31, 2005. Accretion expense reflects the change in the present value of this liability since the end of the prior period. This expense is impacted by factors such as any changes in the estimate of the amount of the future liability for fixed asset removal and nuclear waste management, any changes to the discount rate used to determine the present value, and the change in the present value due to the passage of time.

Accretion expense for 2005 was $467 million compared with $445 million in 2004. The increase in the accretion expense was due to the higher liability base compared to last year as a result of the increase in the present value of the liability due to the passage of time.

Nuclear Fixed Asset Removal and Nuclear Waste Management Funds

OPG is responsible for the ongoing long-term management and disposal of radioactive waste materials and used fuel resulting from operations and future decommissioning of its nuclear generating stations. OPG's obligations relate to the Pickering and Darlington nuclear plants that are operated by OPG, as well as the Bruce A and B nuclear plants that are leased by OPG to Bruce Power.

In order to fund these liabilities, OPG established and manages, jointly with the Province, a Used Fuel Fund and a Decommissioning Fund (the "Nuclear Funds"), which are funded by OPG in accordance with the Ontario Nuclear Funds Agreement ("ONFA"). The Used Fuel Fund is intended to fund future expenditures associated with the disposal of highly radioactive used nuclear fuel bundles. The Decommissioning Fund was established to fund future expenditures associated with nuclear fixed asset removal and the disposal of low and intermediate level nuclear waste materials. OPG maintains the Nuclear Funds in third party custodial accounts that are segregated from the rest of OPG's assets.

Assets in the Nuclear Funds are invested in fixed income and equity securities, which OPG records as long-term investments at their amortized cost. Therefore, gains and losses are recognized only upon the sale of an underlying security. As such, there may be unrealized gains and losses associated with the investments in the Nuclear Funds, which OPG has not recognized in its consolidated financial statements. The balance of the Nuclear Funds on an amortized cost basis, as at December 31, 2005, was $6,788 million compared to $5,976 million as at December 31, 2004. This balance is referred to as the nuclear fixed asset removal and nuclear waste management funds in OPG's consolidated financial statements.

Under ONFA, the Province guarantees the annual rate of return in the Used Fuel Fund at 3.25 per cent plus the change in the Ontario Consumer Price Index ("committed return") over the long term. OPG recognizes the committed return on the Used Fuel Fund and includes it in 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 assets, which includes realized and unrealized returns, is due to or from the Province. Since OPG accounts for the investments in the Nuclear Funds on an amortized cost basis, the amount due to or due from the

Province recorded in the consolidated financial statements is the difference between the committed return and the actual return based on realized returns only. At December 31, 2005, the Used Fuel Fund included an amount due to the Province of $4 million (2004 – $4 million). If the investments in the Used Fuel Fund were accounted for at fair market value in the consolidated financial statements, at December 31, 2005, there would be an amount due to the Province of $306 million (2004 – $156 million). In addition, under ONFA, the Province is entitled to any surplus in the Used Fuel Fund, subject to a threshold funded ratio of 110 per cent compared to the value of the associated liabilities.

Under ONFA, the Decommissioning Fund has a long-term target rate of return of 5.75 per cent per annum. OPG bears the risk and liability for cost estimate increases and fund earnings associated with the Decommissioning Fund. At December 31, 2005, based on the estimate of costs to complete under the current approved ONFA Reference Plan (currently the 1999 Reference Plan), the Decommissioning Fund was fully funded on a market value basis and on an amortized cost basis. When the Decommissioning Fund is overfunded on an amortized cost basis, OPG will limit 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 amortized cost balance of the Decommissioning Fund would equal the cost estimate of the liability based on the 1999 Reference Plan. These realized gains may be recognized in subsequent periods provided the Decommissioning Fund balance declines below the then currently approved cost estimate.

At December 31, 2005, the Decommissioning Fund asset value on an amortized cost basis was $4,099 million compared to a market value of $4,583 million, the difference representing net unrealized gains of $484 million. Under the ONFA, if there is a surplus in the Decommissioning Fund such that the liabilities, as defined by the then current ONFA Reference Plan, are at least 120 per cent funded, OPG may direct up to 50 per cent of the surplus over 120 per cent to be treated as a contribution to the Used Fuel Fund, and the OEFC is entitled to the remaining 50 per cent of such surplus. Any overfunding of the liability is payable to the Province on termination of the Decommissioning Fund. Therefore, the accounting for this overfunded position requires an adjustment to the amortized cost value of the assets in the Decommissioning Fund. This adjustment reduced the value of the assets by $7 million, to equal the value of the liabilities as defined by the current approved ONFA reference plan. If the investments in the Decommissioning Fund were accounted for at fair market value in the consolidated financial statements at December 31, 2005, and the Decommissioning Fund was terminated under the ONFA, there would be an amount due to the Province of $484 million (2004 – $249 million).

Realized earnings on the Nuclear Funds for the year ended December 31, 2005 were $381 million compared to $313 million for 2004, an increase of $68 million. The increase in earnings in 2005 was largely due to higher earnings in the Used Fuel Fund as a result of a larger asset base due to growth through a combination of earnings and contributions, and a higher Ontario CPI compared to 2004.

Regulated – Hydroelectric Segment

(millions of dollars)	**2005**	2004
Revenue, net of Market Power Mitigation Agreement rebate	**792**	824
Fuel expense	**254**	255
Gross margin	**538**	569
Operations, maintenance and administration	**77**	74
Depreciation and amortization	**68**	71
Property and capital taxes	**18**	18
Income before interest, income taxes and extraordinary item	**375**	406

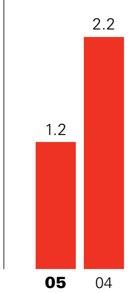
Revenue

(millions of dollars)	**2005**	2004
Spot market sales, net of hedging instruments	**260**	971
Market Power Mitigation Agreement rebate	**(65)**	(194)
Regulated generation sales[1]	**558**	–
Variance accounts	**2**	–
Other	**37**	47
Total revenue	**792**	824

1. Regulated generation sales includes revenue of $210 million that OPG received at the Ontario spot market price for generation over 1,900 MWh in any hour during 2005.

Regulated – Hydroelectric revenue was $792 million for the year ended December 31, 2005 compared to $824 million in 2004. The decrease in revenue was primarily due to lower electricity generation in 2005 of 0.4 TWh compared to 2004, and marginally lower average prices in 2005 due to the introduction of regulated rates and related changes effective April 1, 2005.

Regulated – Hydroelectric EFOR
(%)



Regulated – Hydroelectric OM&A per MWh
($/MWh)

Electricity Prices

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. The average price for the year ended December 31, 2005, was 4.1¢/kWh, after taking into account the regulated price from April 1, 2005 to December 31, 2005, and OPG's average spot market sales price, net of the Market Power Mitigation Agreement rebate for the first quarter of 2005. After taking into account the Market Power Mitigation Agreement rebate, the average spot market sales price for the year ended December 31, 2004 was 4.1¢/kWh.

Volume

Electricity sales volume for the year ended December 31, 2005 was 18.5 TWh compared to 18.9 TWh in 2004. During the period from April 1, 2005 to December 31, 2005, electricity generation of 2.8 TWh related to production levels above 1,900 MWh in any hour. The decrease in generation volume was due to decreased water flows on the Niagara and St. Lawrence rivers during 2005 compared to 2004.

Equivalent forced outage rate (EFOR) for the Regulated – Hydroelectric stations was 1.2 per cent in 2005 compared to 2.2 per cent in 2004. The low EFOR in 2005 and 2004 reflect the high reliability of these stations.

Variance Accounts

OPG is required under a regulation pursuant to the *Electricity Restructuring Act, 2004* to establish variance accounts to capture the impact of certain items during the interim period. One of these items that applies specifically to the Regulated – Hydroelectric segment requires OPG to capture the impact of differences in hydroelectric electricity production due to differences between forecast and actual water conditions. OPG's liability as at December 31, 2005 of $4 million reflected the fact that water conditions were favourable to those forecast. In addition, OPG recorded an asset of $6 million to reflect the fact that actual ancillary revenues were lower than those forecasted.

Fuel Expense

Fuel expense for the year ended December 31, 2005 was $254 million compared to $255 million in 2004. OPG pays charges to the Province and the OEFC on gross revenue derived from the annual generation of electricity from its hydroelectric generating assets. The gross revenue charge ("GRC") includes a fixed percentage charge applied to the annual hydroelectric generation derived from stations located on provincial Crown lands, in addition to graduated rate charges applicable to all hydroelectric stations. GRC costs are included in fuel expense.

Operations, Maintenance and Administration

OM&A expenses for the year ended December 31, 2005 were $77 million compared to $74 million in 2004. OM&A expense per MWh for 2005 increased to $4.17/MWh from $3.92/MWh in 2004 primarily due to the lower generation in 2005 as a result of the reduction in water flows.

Depreciation and Amortization

Depreciation and amortization expense for the year ended December 31, 2005 was $68 million compared to $71 million in 2004.

Unregulated Generation Segment

(millions of dollars)	**2005**	2004
Revenue, net of Market Power Mitigation Agreement and revenue limit rebates	**2,473**	1,942
Fuel expense	**928**	790
Gross margin	**1,545**	1,152
Operations, maintenance and administration	**594**	576
Depreciation and amortization	**276**	302
Accretion on fixed asset removal	**9**	8
Property and capital taxes	**54**	38
Restructuring	**4**	16
Income before the following:	**608**	212
Impairment loss	**202**	–
Income before interest, income taxes and extraordinary item	**406**	212

Revenue

(millions of dollars)	**2005**	2004
Spot market sales, net of hedging instruments	**3,255**	2,417
Market Power Mitigation Agreement rebate	**(187)**	(586)
Revenue limit rebate	**(739)**	–
Other	**144**	111
Total revenue	**2,473**	1,942

Unregulated Generation revenue was $2,473 million for the year ended December 31, 2005 compared to $1,942 million in 2004. The increase in revenue was primarily related to higher average sales prices and higher electricity generation in 2005 compared to 2004. In addition, IESO system constraints related revenue was higher in 2005 compared to 2004.

Electricity Prices

Eighty-five per cent of the generation output from OPG's unregulated generation assets, excluding the Lennox generating station, TRO volumes and forward sales as of January 1, 2005, was subject to a revenue limit based on an average price of 4.7¢/kWh after April 1, 2005. Prior to April 1, 2005, OPG received the average electricity spot market sales price, but revenue was reduced by the Market Power Mitigation Agreement rebate.

OPG's average sales price for its unregulated generation for the year ended December 31, 2005 was 5.4¢/kWh, after taking into account the impact of the revenue limit rebate. The average spot market sales price for the year ended December 31, 2004 was 4.2¢/kWh, net of the Market Power Mitigation Agreement rebate.

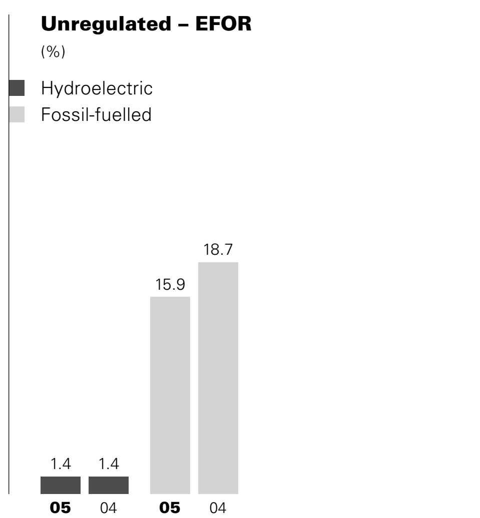
The higher prices during the year ended December 31, 2005 compared to 2004 were due to higher average spot market sales prices during 2005 and the replacement of the Market Power Mitigation Agreement rebate with the revenue limit effective April 1, 2005.

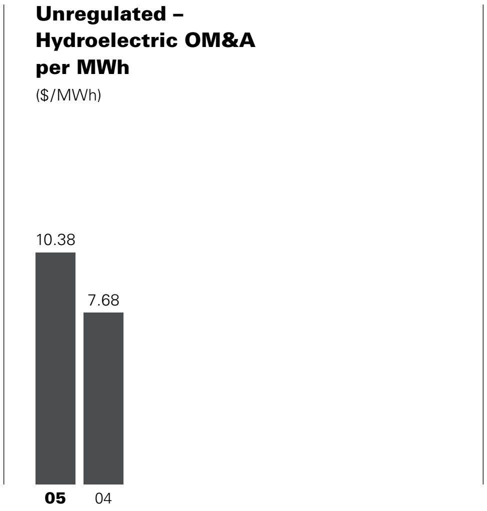
During the period June to December 2005, the Ontario market experienced significantly higher spot market prices which arose from the interaction of a variety of factors. A prolonged period of hot summer weather resulted in increased demand for electricity which required the use of higher marginal cost gas-fired generation. The cost of this gas-fired generation was in turn influenced by higher North American natural gas prices. Also, lower water levels reduced the energy supply from lower marginal cost hydroelectric resources, thereby further increasing the energy to be supplied by higher marginal cost sources. Higher natural gas prices throughout the fall of 2005 continued to affect electricity prices compared to the same period in 2004.

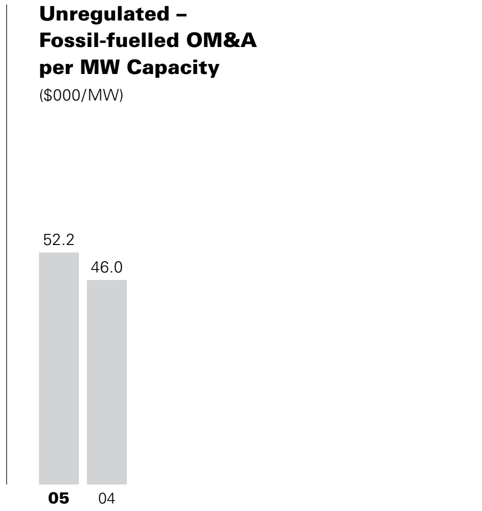
Volume

Electricity sales volume for the year ended December 31, 2005 was 45.0 TWh compared to 43.8 TWh in 2004. Generation from the fossil-fuelled stations increased by 3.9 TWh in 2005 compared to 2004 to meet the higher demand in Ontario. Strong performance from the fossil-fuelled generating stations during 2005 enabled OPG to generate electricity in response to this increased demand. The increase was partly offset by a reduction in volumes of 2.7 TWh from the unregulated hydroelectric facilities due to lower water levels, especially in the Ottawa and northeast regions.

EFOR for the hydroelectric stations remained at 1.4 per cent for both 2005 and 2004, reflecting the continued high reliability of these stations. EFOR for the fossil-fuelled stations decreased to 15.9 per cent in 2005 from 18.7 per cent in 2004, primarily as a result of improved reliability at OPG's Nanticoke generating station.







Fuel Expense

Fuel expense for the year ended December 31, 2005 was $928 million compared to $790 million in 2004. Fuel expense for the Unregulated Generation segment includes the cost of fossil fuels and charges on gross revenue derived from the hydroelectric generating stations. The increase in fuel expense during the 2005 period was primarily due to the higher production from the fossil-fuelled generating stations.

Operations, Maintenance and Administration

OM&A expenses for the year ended December 31, 2005 were $594 million compared to $576 million in 2004. OM&A increased during 2005 as a result of increased maintenance work at OPG's hydroelectric and fossil plants and higher pension and OPEB expenses, partially offset by lower costs from closing the Lakeview generating station.

OM&A expense per MWh for the hydroelectric stations increased to $10.38/MWh in 2005 from $7.68/MWh in 2004 primarily as a result of lower generation in 2005. The higher OM&A expenses also contributed to the increase in OM&A expense per MWh.

OM&A expense per MW ($/MW) for the fossil-fuelled stations increased to $52,200/MW in 2005 from $46,000/MW in 2004 as a result of a decrease in generating capacity with the removal from service of the Lakeview generating station.

Depreciation and Amortization

Depreciation and amortization expense for the year ended December 31, 2005 was $276 million compared to $302 million in 2004. The decrease in expense was primarily due to the extension of the remaining service life of the Nanticoke generating station for purposes of calculating depreciation.

In June 2005, the Province provided further detail on its coal replacement plan. Specific to the Nanticoke generating station, the Province indicated its expectation that the units will be closed through 2008 with the last unit to close in early 2009. As a result, OPG has extended, for purposes of calculating depreciation, the remaining service life of the Nanticoke generating station by one year, from 2007 to 2008. This reduces depreciation expense by approximately $40 million annually over the period to 2007.

Impairment of Long-Lived Assets – Lennox Generating Station

The Lennox generating station has available generating capacity in excess of 2,000 MW. It is available to provide operating reserve, and has dual fuel capability with natural gas and oil. The Lennox generating station has annual fixed operating costs of about $60 million. Since the formation of OPG in 1999, revenue earned from electricity generated at the Lennox station was generally not sufficient to cover the fixed operating costs and annual depreciation charge related to the station. However, up until 2004, OPG expected that in the future, demand for new electricity supply requirements in Ontario would require the development of a capacity market or higher market prices sufficient for new entrants to cover their costs and provide a return on investment. As a result, revenues associated with the Lennox generating station were expected to be sufficient to cover all costs, including a recovery of the carrying value.

In 2004, the Government issued a "Request for Information/ Request for Proposal for 2,500 MW of New Clean Generation and Demand Side Management Projects" under which new generators would be allowed to recover fixed costs and an agreed upon rate of return on investment through contractual arrangements. By recovering these costs through contractual arrangements with the OPA, new entrants would need to recover only fuel and other variable operating costs from the wholesale market. These contracts are expected to result in lower than anticipated future revenue from the wholesale electricity market.

As a relatively high cost plant, the Lennox generating station likely will not be able to recover its fixed operating costs and the carrying value from the wholesale market in the future. Given these factors, and the precedent established under the Request for Information/Request for Proposal for 2,500 MW, OPG had initiated discussions with the Province, with the intention of entering into a contractual arrangement for the recovery of the annual fixed operating costs of about $60 million and the carrying value of the Lennox generating station over its remaining estimated useful life of $17 million per year.

OPG followed up on the discussions with the Province concerning the Lennox generating station situation by engaging in discussions with the IESO during the first quarter of 2005. OPG expected that it would be able to negotiate an arrangement that would provide for the recovery of all costs. Subsequently, OPG was advised by the Province that while it would continue to support OPG's negotiations with the IESO regarding the recovery of fixed operating costs, it would not support an arrangement that would allow for the recovery of costs related to the carrying value of the Lennox generating station. As a result of the change in circumstance, OPG recorded an impairment loss of $202 million during the first quarter of 2005, which was the amount of the carrying value of the generating station before the impairment loss. OPG has since negotiated a contract with the IESO pursuant to the market rules to recover its operating costs for a one-year period ending September 30, 2006. The contract with the IESO has been submitted to the OEB for approval.

Other

(millions of dollars)	**2005**	2004
Revenue	**86**	105
Operations, maintenance and administration	**57**	62
Depreciation and amortization	**35**	32
Property and capital taxes	**4**	14
Restructuring	**6**	4
Other income	**–**	(8)
(Loss) income before interest and income taxes and extraordinary item	**(16)**	1

Revenue

Other revenue was $86 million during the year ended December 31, 2005 compared to $105 million in 2004. The decrease of $19 million in 2005 compared to 2004 was primarily related to a decrease in trading revenue, partly offset by an increase in revenue from OPG's joint venture share in Brighton Beach. Brighton Beach went into service in July 2004.

Trading revenue for the year ended December 31, 2005 was $17 million compared to trading revenue of $47 million in 2004. The decrease of $30 million during 2005 compared to 2004 was primarily due to mark-to-market losses on long-term contracts outside of Ontario, which were arranged by OPG's predecessor company, Ontario Hydro. During 2005, a decrease in realized trading margin also contributed to lower trading revenue compared to 2004.

Interconnected purchases and sales (including those to be physically settled) and mark-to-market gains and losses (realized and unrealized) 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 year ended December 31, 2005 would have increased by $228 million (2004 – $170 million), with no impact on net income.

The carrying amounts and notional quantities of derivative instruments not designed for hedging purposes are disclosed in Note 12 in the audited consolidated financial statements.

Net Interest Expense

Net interest expense for 2005 was $197 million compared to $189 million in 2004. The increase in net interest expense of $8 million during 2005 was mainly due to higher long-term debt in 2005, partially offset by an increase in interest income as a result of higher cash on hand and short-term investments in 2005, and an increase in interest capitalized.

Income Taxes

Commencing April 1, 2005, with the introduction of rate regulation, OPG accounts for income taxes relating to the rate regulated segments of its business using the taxes payable method. Under the taxes payable method, OPG does not recognize future income taxes relating to the rate regulated segments of its business to the extent those future income taxes are expected to be recovered in the regulated rates charged to future customers. For all other operations, the liability method of tax accounting is followed. 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.

Income tax expense for the year ended December 31, 2005 was $118 million compared to an $80 million income tax recovery in 2004. During 2005, OPG recorded an income tax charge of $50 million to provide for a change in income tax liabilities related to certain income tax positions that the Company has taken in prior years. During 2005, the income tax expense was $157 million lower than what would otherwise have been recorded, due to the application of the taxes payable method for the regulated segments.

As a result of the adoption of the taxes payable method for the rate regulated segments on April 1, 2005, OPG eliminated the net future income tax asset balance of $74 million relating to the rate regulated segments and recognized the amount as a one-time extraordinary loss in determining net income.

Prior to 2004, OPG had established a valuation allowance of $93 million to recognize that it was more likely than not that this amount of future income taxes recoverable would not be realized in light of consecutive taxable losses in preceding years. In 2004, the valuation allowance was reduced by $93 million to nil as a consequence of the introduction of rate regulation. With the intended elimination of the future income tax assets and liabilities of the regulated business upon inception of rate regulation on April 1, 2005, it was expected that there would be a significant future income tax liability position remaining in the unregulated business. This expected future income tax liability position enabled OPG to recognize, in 2004, the $93 million in future income tax assets. This resulted in a reduction in the 2004 income tax provision, which did not recur in 2005.

Proxy Property Taxes

In November 2005, OPG received a letter from the Ministry of Finance indicating its intent to recommend to the Minister of Finance that an Ontario regulation covering proxy property taxes be updated retroactive to April 1, 1999, to reflect reassessments and appeal settlements of certain OPG properties since that date. Updates to the regulation may not occur for up to two years. OPG has not recorded any amounts relating to this anticipated regulation change.

Liquidity and Capital Resources

OPG's primary sources of liquidity and capital are funds generated from operations, bank financing and credit facilities provided by OPG's Shareholder. These resources are required for continued investment in plant and technologies, and to meet other significant funding obligations including contributions to the pension fund and the Nuclear Funds, and to service and repay long-term debt and revenue limit rebate obligations.

Years ended December 31 (millions of dollars)	**2005**	2004	Explanation
Cash and cash equivalents, beginning of year	**2**	286	
Cash flow provided by (used in):			
Operating activities	**1,201**	226	Increase in cash from operating activities primarily due to higher sales revenue and earnings in 2005 compared to 2004, and lower rebate payments.
Investing activities	**(760)**	(543)	Increase in cash used in investing activities due to the treatment of non-capital expenses related to the Pickering A return to service project as a regulatory asset in 2005, partially offset by a decrease in investment in fixed assets.
Financing activities	**465**	33	Increase in cash from financing activities due primarily to issuance of long-term debt in 2005, partially offset by a net decrease in the issue of short-term notes.
Net increase (decrease)	**906**	(284)	
Cash and cash equivalents, end of year	**908**	2	

Operating Activities

Net cash from operating activities was $1,201 million for the year ended December 31, 2005 compared to $226 million in 2004. The increase in cash flow from operating activities in 2005 was primarily due to higher revenue and earnings in 2005 as a result of the increase in OPG's average sales prices and generation, and reduced Market Power Mitigation Agreement rebate payments in 2005. These favourable impacts on net cash from operating activities were partially offset by an increase in pension contributions in 2005 compared to 2004.

OPG made rebate payments of $851 million during 2005 under the Market Power Mitigation Agreement compared to payments of $1,124 million during 2004. The Market Power Mitigation Agreement was terminated as of March 31, 2005. Under this Agreement, OPG paid rebates totalling $4 billion between May 1, 2002, when the Ontario market opened to competition, and December 31, 2005, resulting in a significant unfavourable impact on OPG's liquidity.

Under the revenue limit rebate, which was introduced effective April 1, 2005, OPG is required to rebate $739 million in 2006, representing the generation output subject to the revenue limit of 4.7¢/kWh for the period between April 1, 2005 and December 31, 2005. Additional revenue limit rebates incurred between January 1, 2006 and April 30, 2006 will be paid in 2006, along with additional rebate payments as a result of the extension of the revenue limit beyond April 30, 2006.

OPG made contributions of $254 million to the pension plan in 2005 compared to $154 million in 2004. Pension contributions were increased in 2005 to reflect funding requirements based on a January 1, 2005 actuarial valuation of the pension plan.

As required under ONFA, OPG made total contributions of $454 million to the nuclear fixed asset removal and nuclear waste management funds in 2005 and 2004.

Investing Activities

OPG is in a capital-intensive business that requires continued investment in plant and technologies to improve generating asset performance through production efficiencies and increased reliability, increase the generating capacity of existing stations, add new generating capacity, and maintain and improve the safety and environmental performance of its assets. Capital expenditures during the year ended December 31, 2005 were $498 million compared with $561 million in 2004. The decrease in capital expenditures was due to a reduction in Pickering A return to service and environmental qualification capital expenditures in 2005 and the completion of construction activity at Brighton Beach in 2004, partially offset by expenditures on the Niagara tunnel. OPG's anticipated capital expenditures for 2006 are expected to increase to approximately $850 million, primarily as a result of the Niagara tunnel project and expenditures related to the Lac Seul and Thunder Bay generating station projects.

Financing Activities

OPG renewed its $1 billion revolving committed bank credit facility as of May 2005. The renewed facility is divided into two tranches – a $500 million 364-day term tranche maturing in May 2006 and a $500 million three-year term tranche maturing in May 2008. The total credit facility will continue to be used primarily as credit support for notes issued under OPG's commercial paper program. As at December 31, 2005, OPG had no borrowing outstanding under its commercial paper program compared to $26 million outstanding as at December 31, 2004. OPG has not borrowed under its commercial paper program since April 2005. As at December 31, 2005, OPG had no other outstanding borrowing under its bank credit facility.

OPG maintains $26 million (2004 – $26 million) in short-term uncommitted bank operating credit facilities as well as $215 million (2004 – $200 million) of other short-term uncommitted credit facilities, to support the issuance of Letters of Credit. OPG uses Letters of Credit to support its supplementary pension plans, and is required to post Letters of Credit as collateral with Local Distribution Companies ("LDCs") as required under the Market Rules (Ontario Energy Board's Retail Settlement Code). At December 31, 2005, there was a total of $157 million (2004 – $155 million) of Letters of Credit issued, $138 million relating to supplementary pension plans and $19 million relating to collateral requirements to the LDCs.

In March 2005, the Company reached an agreement with the OEFC to obtain additional long-term financing for up to $600 million. The financing was required to meet a projected operating cash shortfall. In April 2005, $400 million was advanced under this facility for a seven-year term. In accordance with the OEFC Agreement, the remaining $200 million of additional financing is available to be drawn up to March 31, 2006.

In March 2005, OPG issued a note of $95 million to the OEFC. This financing was used for payment of OPG's interest obligation to the OEFC.

In September 2005, OPG reached an agreement with the OEFC to finance the Niagara tunnel construction project. The funding, of up to $1 billion, will be advanced in the form of 10-year notes, on commercial terms and conditions, over the duration of the project to meet the project's obligations. Advances under this facility are expected to commence in the second quarter of 2006.

In October 2005, OPG reached a similar agreement with the OEFC to finance the Thunder Bay Gas Conversion project. There is up to $95 million available to OPG under this credit facility that will be drawn as needed over the projected two-year construction period. OPG is expected to make its first draw under this facility in the first quarter of 2006.

As at December 31, 2005, OPG's long-term debt outstanding with the OEFC was $3.7 billion. Although the new financing added in 2005 has extended the maturity profile, $3 billion of long-term debt must be repaid or refinanced within the next five years.

Contractual and Commercial Commitments

The Company's contractual obligations and other significant commercial commitments as at December 31, 2005 are as follows:

(millions of dollars)	2006	2007	2008	2009	2010	Thereafter	Total
Contractual obligations:							
Fuel supply agreements	693	425	197	68	15	15	**1,413**
Contributions under ONFA	454	454	679	350	350	1,403	**3,690**
Long-term debt repayment	800	400	400	350	970	775	**3,695**
Interest on long-term debt	214	168	145	122	90	55	**794**
Unconditional purchase obligations	26	20	12	9	15	27	**109**
Long-term accounts payable	28	28	9	–	–	–	**65**
Operating lease obligations	13	13	13	13	14	–	**66**
Pension contributions[1]	254	–	–	–	–	–	**254**
Other	75	34	35	34	35	11	**224**
Significant commercial commitments:							
Niagara Tunnel	158	173	172	116	1	–	**620**
Total	2,715	1,715	1,662	1,062	1,490	2,286	**10,930**

1. The pension contributions include additional funding requirements towards the deficit and ongoing funding requirements in accordance with the actuarial valuation as at January 1, 2005. The contributions are affected by various factors including market performance, changes in actuarial assumptions, plan experience, and the timing of funding valuations. Funding requirements after 2006 are excluded due to significant variability in the assumptions required to project the timing of future cash flows.

Credit Ratings

Maintaining an investment grade credit rating is essential for corporate liquidity, and cost effective capital market access. At December 2005, OPG has a long-term credit rating of BBB+ by Standard & Poor's ("S&P") and A (low) by Dominion Bond Rating Service ("DBRS"). In May 2005, following a review of the new interim regulatory framework in which OPG will operate, DBRS changed the trend on OPG's unsecured debt from negative to stable and confirmed the rating on OPG's commercial paper at R-1 (low). In September 2005, S&P revised OPG's rating outlook from developing to positive, and confirmed OPG's BBB+ long-term corporate credit rating and short-term A-2 commercial paper rating.

Critical Accounting Policies and Estimates

OPG's significant accounting policies, including the impact of future accounting pronouncements, are outlined in Note 3 to the consolidated financial statements as at and for the year ended December 31, 2005. Certain of these policies are recognized as critical accounting policies by virtue of the subjective and complex judgments and estimates required around matters that are inherently uncertain and could result in materially different amounts being reported under different conditions or assumptions. The critical accounting policies and estimates that affect OPG's consolidated financial statements, the likelihood that materially different amounts would be reported under varied conditions and estimates and the impact of changes in certain conditions or assumptions, are highlighted below.

Rate Regulated Accounting

A regulation made pursuant to the *Electricity Restructuring Act, 2004* prescribes that OPG's nuclear and baseload hydroelectric facilities receive regulated prices for their output. Under this regulation, OPG is required to establish a deferral account in connection with non-capital costs incurred on or after January 1, 2005 that are associated with the return to service of units at the Pickering A nuclear generating station. As at December 31, 2005, the deferral account balance was $261 million, consisting of non-capital costs of $228 million related to Unit 1, $19 million related to Units 2 and 3, $11 million of general return to service costs and interest of $7 million accreted at the average cost of debt of six per cent. OPG commenced the amortization of the deferral account associated with Unit 1 of the Pickering A nuclear generating station when the unit was returned to service in November 2005. The amortization of $4 million was charged to OM&A expense. Upon OPG becoming subject to regulated prices established by the OEB in 2008, the OEB is directed by the regulation to ensure that OPG recovers any balance in the deferral account through rates charged to future customers on a straight-line basis, over a period not to exceed 15 years.

In addition, under the regulation, OPG is required to establish an account to record certain variances from forecast, incurred on or after April 1, 2005, associated with a number of predefined circumstances. Under the terms of the regulation, the OEB is directed to ensure that OPG recovers those amounts, which have been prudently incurred and accurately recorded, through rates charged to future customers over a period not to exceed three years. Conversely, OPG will return to customers, where appropriate, certain other variance amounts recorded in this account. As at December 31, 2005, OPG had recorded a regulatory liability of $4 million in a variance account reflecting water conditions that were favourable to those forecasted. Other regulatory liability consists of a portion of non-regulated revenue earned by OPG's regulated assets, which will result in a reduction of future regulated rates to be established by the OEB. OPG also had recorded a regulatory asset of $5 million related to revenues for ancillary services that were below the forecast used to establish regulated rates. The measurement of regulatory assets and liabilities are subject to certain estimates and assumptions including assumptions made in the interpretation of the regulation.

With the commencement of rate regulation for OPG's baseload hydroelectric and nuclear facilities on April 1, 2005, OPG recorded an extraordinary loss of $74 million resulting from the elimination of the net future income tax asset.

Income Taxes

OPG is exempt from tax under the *Income Tax Act* (Canada). However, under the *Electricity Act, 1998,* OPG is required to make payments in lieu of corporate income and capital taxes to the OEFC. These payments are calculated in accordance with the *Income Tax Act* (Canada) and the *Corporations Tax Act* (Ontario), and are modified by regulations made under the *Electricity Act, 1998*.

OPG's operations are complex and the computation of the provision for income taxes involves interpretation of the various tax statutes and regulations. The *Income Tax Act* (Canada) and the *Corporations Tax Act* (Ontario) have a large body of technical interpretations and case law to help determine the Company's filing position. However, the *Electricity Act, 1998,* and tax related regulations are relatively new and it was therefore necessary for OPG to take certain filing positions in calculating the amount of the income tax provision. These filing positions may be challenged on audit and possibly disallowed, resulting in a potential significant increase in OPG's tax provision upon reassessment. Although management believes that it has adequately provided for income taxes based on all information currently available, there is uncertainty given how recently the legislation was introduced.

OPG uses the liability method of accounting for income taxes for the unregulated segment of the business and provides future income taxes for income tax temporary differences. The process involves an estimate of OPG's actual current tax liability and an assessment of the Company's future income taxes as a result of temporary differences arising from the difference between the tax basis of an asset or liability and its carrying value on the consolidated balance sheet. In addition, OPG has to assess whether the future tax assets can be realized and to the extent that recovery is not considered likely, a valuation allowance must be established. Judgment is required in determining the provision for income taxes, future income tax assets and liabilities and any related valuation allowance. To the extent a valuation allowance is created or revised, current period earnings will be affected.

Commencing April 1, 2005, OPG accounts for income taxes related to the rate regulated segments of its business in accordance with paragraphs 102 to 104 inclusive of the Canadian Institute of Chartered Accountants ("CICA") handbook, Section 3465 – Income Taxes. Accordingly, OPG does not recognize future income taxes related to the rate regulated segments of its business to the extent that these income taxes are expected to be recovered in the regulated rates charged to future customers.

Future tax assets of $269 million have been recorded on the consolidated balance sheet at December 31, 2005. The Company believes there will be sufficient future taxable income and capital gains that will permit the use of these deductions and carry-forwards. Because of the adoption of rate regulated accounting, OPG did not record future tax assets of $3,297 million, which it would have recorded under the liability method, resulting primarily from temporary differences related to the nuclear fixed asset removal and nuclear waste management provisions.

Future tax liabilities of $492 million have been recorded on the consolidated balance sheet at December 31, 2005. Because of the adoption of rate regulated accounting, OPG did not record future tax liabilities of $3,380 million, which it would have recorded under the liability method, resulting primarily from temporary differences related to the nuclear fixed asset removal and nuclear waste management fund.

Business Segments

Prior to April 1, 2005, OPG had two reportable business segments: Generation and Energy Marketing. A separate category, Other, included revenue and certain expenses that were not allocated to its business segments. With the introduction of rate regulation, OPG changed the definition of its reportable business segments in order to remain compliant with the CICA handbook, Section 1701 – Segment Disclosure. OPG reports its results on the basis of these new segments beginning April 1, 2005 and has reclassified prior period amounts accordingly.

Impairment of Generating Stations and Other Fixed Assets

OPG's business is capital intensive and requires significant investment in property, plant and equipment ("fixed assets"). At December 31, 2005, the net book value of OPG's fixed assets was $11,412 million.

Property, plant and equipment are tested for recoverability whenever events or changes in circumstances indicate that the carrying amounts may not be recoverable. Recoverability of property, plant and equipment is determined by comparing the carrying amount of an asset to the undiscounted future net cash flows expected to be generated from the asset over its estimated useful life. In cases where the undiscounted expected future cash flows are less than the carrying amounts, an impairment loss is recognized equal to the amount by which the carrying amount exceeds the fair value, or discounted cash flows.

Various assumptions and accounting estimates are required to determine whether an impairment loss should be recognized and, if so, the value of such loss. This includes factors such as short-term and long-term forecasts of the future market price of electricity, the demand for and supply of electricity, the in-service dates of new and laid-up generating stations, inflation, fuel prices, capital expenditures and station lives. The amount of the future net cash flow that OPG expects to receive from its fixed assets could differ materially from the net book values recorded in OPG's consolidated financial statements.

Pension and Other Post Employment Benefits

OPG's accounting for pension and other post employment benefits are dependent on management's accounting policies and assumptions used in calculating such amounts.

Accounting Policy

In accordance with Canadian generally accepted accounting principles, actual results that differ from the assumptions used, as well as adjustments resulting from changes in assumptions, are accumulated and amortized over future periods and therefore generally affect recognized expense and the recorded obligation in future periods.

Under OPG's policy on accounting for pension and OPEB, certain actuarial gains and losses have not been charged to expense and are therefore not reflected in OPG's pension and OPEB obligations as a result of the following:

- Pension fund assets are valued using market-related values for purposes of determining actuarial gains or losses and the expected return on plan assets. The market-related value recognizes gains and losses on equity assets relative to a six per cent assumed real return over a five-year period.
- For pension and OPEB, the excess of the net cumulative unamortized gain or loss, over 10 per cent of the greater of the benefit obligation and the market-related value of the plan assets (the "corridor"), is amortized over the expected average remaining service life.

In addition, past service costs arising from pension and OPEB plan amendments are amortized over future periods and therefore affect recognized expense and the recorded obligation in future periods.

At December 31, 2005, the unamortized net actuarial loss and unamortized past service costs for the pension plan and other post employment benefits amounted to $2,760 million (2004 – $1,604 million). Details of the unamortized net actuarial loss and total unamortized past service costs at December 31, 2005 and 2004 are as follows:

	Registered Pension Plan		Supplementary Pension Plans		Other Post Employment Benefits	
(millions of dollars)	**2005**	2004	**2005**	2004	**2005**	2004
Net actuarial loss (gain) not yet subject to amortization due to use of market-related values	**(48)**	476	**–**	–	**–**	–
Net actuarial loss not subject to amortization due to use of corridor	**910**	536	**14**	14	**207**	150
Net actuarial loss subject to amortization	**875**	–	**4**	14	**678**	272
Unamortized net actuarial loss	**1,737**	1,012	**18**	28	**885**	422
Unamortized past service costs	**100**	119	**4**	5	**16**	18

Accounting Assumptions

Assumptions used in determining projected benefit obligations and the costs for the Company's employee benefit plans are evaluated periodically by management in consultation with an independent actuary. Critical assumptions such as the discount rate used to measure the Company's benefit obligations, the expected long-term rate of return on plan assets and health care cost projections are evaluated and updated annually. The discount rates used by OPG in determining projected benefit obligations and the costs for the Company's employee benefit plans are based on representative AA corporate bond yields.

A change in these assumptions, holding all other assumptions constant, would increase (decrease) 2005 costs, excluding amortization components, as follows:

(millions of dollars)	Registered Pension Plan	Supplementary Pension Plans	Other Post Employment Benefits
Expected long-term rate of return			
0.25% increase	(19)	na	na
0.25% decrease	19	na	na
Discount rate			
0.25% increase	(10)	–	(2)
0.25% decrease	11	–	2
Inflation			
0.25% increase	31	1	na
0.25% decrease	(29)	(1)	na
Salary increases			
0.25% increase	7	2	–
0.25% decrease	(7)	(1)	–
Health care cost trend rate			
1% increase	na	na	26
1% decrease	na	na	(20)

na – change in assumption not applicable

Asset Retirement Obligations

OPG's asset retirement obligations are comprised of liabilities for nuclear fixed asset removal and nuclear waste management costs and non-nuclear fixed asset removal costs related to the decommissioning of fossil-fuelled generating stations. The liabilities associated with decommissioning the nuclear generating stations and long-term used nuclear fuel management comprise the most significant amounts of the total obligation. The estimates of the nuclear liabilities are reviewed on an annual basis as part of the ongoing, overall nuclear waste management program. Changes in the nuclear liabilities resulting from changes in assumptions or estimates that impact the amount of the originally estimated undiscounted cash flows are recorded as an adjustment to the liabilities, with a corresponding change in the related asset retirement cost capitalized as part of the carrying amount of the long-lived asset.

The estimates of nuclear fixed asset removal and nuclear waste management costs require significant assumptions in the calculations since the programs run for many years. Significant assumptions underlying operational and technical factors are used in the calculation of the accrued liabilities and are subject to periodic review. Changes to these assumptions, including changes in the timing of programs, technology employed, inflation rate, and discount rate, could result in significant changes in the value of the accrued liabilities.

The current estimate of costs to complete the nuclear fixed asset removal and nuclear waste management is in accordance with the current approved reference plan. OPG is currently performing a detailed review, which will result in an updated reference plan. It is expected that this updated reference plan will be completed and approved during 2006.

With the return to service of Unit 1 at the Pickering A nuclear generating station and the decision in 2005 not to restart Units 2 and 3, OPG is reviewing the impact that these events will have on the assumptions, changes in timing to programs and the estimated costs underlying the accrued nuclear fixed asset removal and nuclear waste management liability. Any resulting changes to the estimated accrual will be reflected in the planned update to the reference plan in 2006.

Depreciation

Property, plant and equipment for OPG's generating stations are depreciated based on their estimated service lives on a straight-line basis. The service lives of the generating stations are estimated based on expected consumption, government legislation and management intent.

In June 2005, the Province provided further details on its coal replacement plan. Hence, effective in July 2005, OPG extended, for purposes of calculating depreciation, the remaining service life of the Nanticoke generating station for one year to December 2008. This change in estimate was accounted for on a prospective basis and reduced the depreciation expense by $20 million in 2005.

OPG has also extended, for purposes of calculating depreciation, the remaining service life of the Pickering A nuclear generating station Unit 4 from 2017 to the year 2021, consistent with the remaining service life of Unit 1. This change reflects management's assessment of the remaining service life, taking into account the recent refurbishment of this unit. This change was effective in November 2005 and reduces depreciation expense by approximately $16 million annually over the period to 2017, excluding the impact of future asset additions planned at the station.

OPG will continue to review the estimated useful lives of its generating stations including the Pickering B Units. Any changes resulting from the review will be reflected in 2006.

Risk Management

OPG's portfolio of generation assets and its electricity trading and marketing operations are subject to inherent risks, including financial, operational, and strategic risks. To manage these risks, OPG's Board of Directors and management have implemented an integrated enterprise-wide risk management framework for the governance, identification, measurement, monitoring and reporting of risk across all of OPG and its business operations. Implementation and coordination of corporate-wide risk management activities are undertaken 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 management group, and is reported by the Chief Risk Officer to the Audit and Risk Committee of the Board of Directors on a routine basis. Risk based processes are incorporated into strategic and financial planning to ensure the Company's sustainability and achievement of its stated objectives.

While OPG believes it is pursuing appropriate risk management strategies, there can be no assurance that one or more of the risks outlined or other risk factors will not have a material adverse impact on OPG. In particular, the *Electricity Restructuring Act, 2004* and related regulations, the imposition of a revenue limit on the non-regulated assets excluding the Lennox generating station and volumes related to existing contracts, and changes in the future mandate of OPG in the Ontario electricity marketplace could have a material impact on OPG.

Risk Classification

For purposes of tracking and communicating risk information, the Company uses the following three major risk categories including:

- Financial Risk: the risk of financial loss caused by external market factors, including market prices and volatilities, credit, foreign exchange, interest rate, liquidity and other factors,
- Operational Risk: the risk of direct or indirect loss resulting from external events or from inadequate or failed internal processes, people, equipment and systems. These include changes in generation reliability, fuel supply and availability, security, business process risks, business interruption, human resources risks and information technology risks, and
- Strategic Risk: the risk that adverse events or conditions in OPG's regulatory, economic, political and social environment will prevent OPG from achieving its objectives. These include risks from adverse regulatory changes or onerous existing regulations; risks from unexpected economic conditions; the risk of financial loss or damaged reputation resulting from unexpected political actions; and succession planning risk.

Risk Management Tools

In addition to qualitative indicators provided through risk-based internal audits, reviews and self-assessments, OPG uses quantitative tools and metrics for monitoring and managing risks. OPG continuously assesses the appropriateness and reliability of risk management tools and metrics in light of the changing risk environment. Some of the tools and metrics that OPG currently uses to measure and report on risk are:

- Business Unit Risk Self-assessments (BURSA©) are conducted across the Company annually, and updated quarterly. Using standard criteria for assessing the probability and consequence of risk events, OPG business units assess the risks in their processes, operations and projects. The output from the BURSA process helps the business units develop risk mitigation plans to avoid, transfer, reduce or accept the risk and make risk-based capital allocation decisions,
- Value-at-Risk (VaR) analysis is used to measure and manage market risks in OPG's electricity trading portfolio. The VaR approach is used to derive a quantitative measure specifically for market risks under normal market conditions. 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,
- Stress tests help to determine the effects of potentially extreme market developments on the market values of electricity trading and marketing positions. Stress testing is used to determine the amount of economic capital OPG needs to allocate to cover market risk exposure under extreme market conditions, and
- Economic capital is a measure of the amount of equity capital needed at any given date to absorb unexpected losses arising from exposures on that date. Currently, OPG calculates credit economic capital in relation to Energy Markets activities.

Financial Risk

Commodity Price Risk

Commodity price risk is the risk that changes in the market price of electricity or of the fuels used to produce electricity will 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 opportunity to do so in an economically justified manner. To manage the input risk, OPG has a fuel hedging program. In addition to fixed price contracts for fossil and nuclear fuels, OPG periodically employs derivative instruments to hedge its fuel price risk.

Through a regulation passed pursuant to the *Electricity Restructuring Act, 2004,* OPG receives regulated prices for its baseload hydroelectric and nuclear facilities (approximately 60 per cent of OPG generation) from April 1, 2005. These prices are expected to remain in effect until at least March 31, 2008, or until such time that the OEB establishes new regulated prices. Eighty-five per cent of the remaining unregulated OPG electricity generation, excluding generation from the Lennox generating station and volumes relating to existing contracts, is subject to a revenue limit of 4.7¢/kWh, in place from April 1, 2005 to April 30, 2006. The Government recently announced the extension of this revenue limit for an additional three years.

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

	2006	2007	2008
Estimated generation output hedged[1]	92%	92%	93%
Estimated fuel requirements hedged[2]	97%	89%	77%
Estimated nitric oxide (NO) emission requirement hedged[3]	100%	77%	68%
Estimated sulphur dioxide (SO_2) emission requirement hedged[3]	100%	100%	100%

1. 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 the transition rate option contracts, regulated price for baseload hydroelectric and nuclear generation, and revenue limit for non-prescribed assets.
2. 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.
3. 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 Regulations 397/01.

Open trading positions are subject to measurement against Value at Risk ("VaR") limits. VaR utilization ranged between $0.7 million and $3.0 million during the year ended December 31, 2005, compared to $0.4 million and $2.2 million during the year ended December 31, 2004. VaR utilization is within the risk tolerance of the Company, under approved VaR limits.

Trading liquidity continues to be constrained in Ontario and interconnected markets due to broader energy market fundamentals. In addition, the revenue limit reduces customer exposure to electricity spot market prices and further limits trading liquidity.

Credit Risk

Credit risk is the financial risk of non-performance by contractual counterparties. Credit risk excludes any operational risk resulting from a third party failing to deliver a product or service as expected. OPG derives revenue from several other sources including the sale of energy products and financial risk management products to third parties. However, the majority of OPG revenues are derived from sales through the IESO-administered spot market.

Credit exposure to the IESO fluctuates based on spot prices and the volume of rate regulated and unregulated generation, and is reduced each month upon settlement of the accounts. Credit exposure to the IESO peaked at $1,146 million during the year ended December 31, 2005 and at $901 million during the year ended December 31, 2004.

OPG's management believes that the IESO is an acceptable credit risk due to its primary role in the Ontario market. The IESO manages its own credit risk and its ability to pay generators by mandating that all registered IESO spot market participants meet specific IESO standards for creditworthiness and collateralization. Additionally, in the event of an IESO participant default, each market participant shares the exposure pro rata. Given OPG's position in the marketplace, the Company would bear approximately 35 per cent of the exposure, residual of collateral and recovery.

OPG also monitors and reports its credit exposure with counterparties. OPG's management believes these are within acceptable limits and does not anticipate any material effect on its results of operations or cash flows arising from potential defaults.

The following table provides information on credit risk from energy sales and trading activities as at December 31, 2005:

			Potential Exposure for Largest Counterparties	
Credit Rating[1]	Number of Counterparties[2]	Potential Exposure[3]	Number of Counterparties	Counterparty Exposure
		(millions of dollars)		(millions of dollars)
AAA to AA-	38	3	–	–
A+ to A-	44	37	1	15
BBB+ to BBB-	85	32	1	10
BB+ to BB-	27	145	7	135
Below BB-	32	62	1	59
Subtotal	226	279	10	219
IESO	1	661	1	661
Total	227	940	11	880

1. 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.
2. OPG Counterparties are defined by each Master Agreement.
3. Potential exposure is OPG's assessment of the maximum exposure over the life of each transaction at 95 per cent confidence.

For all counterparties, OPG's contracts allow for active collateral management to mitigate credit exposures. The contracts provide for a counterparty to post performance guarantees in excess of the established threshold. OPG may employ such guarantees as a result of market price changes or upon the occurrence of credit-related events. The threshold amount represents credit limits established in accordance with the corporate credit policy. Inability to post collateral is sufficient cause to terminate a contract and liquidate all positions.

Liquidity Risk

OPG operates in a capital intensive business. Significant financial resources are required to fund capital improvement projects and maintenance at generating stations and potential expenditures necessary to comply with environmental or other regulatory requirements. In addition, the Company has other significant disbursement requirements including rebate payments associated with the revenue limit, annual funding obligations under ONFA, pension funding and continuing debt maturities with the OEFC. A discussion of corporate liquidity is included in the Liquidity and Capital Resources section.

Foreign Exchange and Interest Rate Risk

OPG's foreign exchange exposure is attributable to two primary factors: U.S. 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, impacting OPG's revenues. The magnitude and direction of the exposure to the USD from OPG's operations is impacted by generation reliability and the price volatility of USD denominated commodities. OPG currently manages its exposure using forwards and other derivative products to periodically hedge portions of its anticipated USD exposures according to approved risk management policies.

OPG has interest rate exposure on its short-term borrowings and investment programs. The majority of OPG's existing debt is fixed on a long-term basis. Interest rate risk arises with the need to undertake new financing and with the potential addition of variable rate debt. Interest rate risk may be hedged using derivative instruments. The management of these risks is undertaken by selectively hedging in accordance with corporate risk management policies.

Operational Risk

Generation Risk

OPG is exposed to the financial impacts of uncertain output from its generating units. The amount of electricity generated by OPG is affected by fuel supply, equipment malfunction, maintenance requirements, and regulatory and environmental constraints. To mitigate earnings volatility due to generation risk, OPG enters into multiple short-term and long-term fuel supply agreements and long-term water use agreements, manages fuel supply inventories, and follows industry practices for maintenance and outage scheduling. In addition, OPG ensures regulatory requirements are met, particularly with respect to licensing of its nuclear facilities, and manages environmental constraints utilizing programs such as emission reduction credits.

OPG is exposed to considerable technology risk around the aging of the nuclear fleet. Technology risks that could lead to significant impacts on the production capability or operating life of these assets are not fully predictable and OPG attempts to identify and mitigate these risks through ongoing management review and assessments, internal audits and from experience of nuclear units around the world. OPG has undertaken an ongoing life cycle management program to assess the condition of major components of the nuclear units, including steam generators, fuel channels and feeder pipes, and address the active degradation mechanisms associated with these major components. Current predictions for unit end of life are based on the end of life predictions for the fuel channels.

Thinning of the carbon steel feeder pipes used to transport the hot pressurized water in the reactor to the steam generators is an industry-wide issue. Thinning of feeder pipes occurs to varying degrees at all of OPG's reactors. While this condition affects all of OPG's nuclear generating stations, it is most significant at the Darlington nuclear generating station. Mitigation options are under development by OPG which may extend feeder pipe life, reduce the thinning rate, and improve the capability to replace feeders, where required. Recent wall thickness measurements of removed feeders and field inspections at Pickering A Units 1 and 4 have indicated that the location of the thinning is different than at Darlington, and the degree of thinning is greater than originally expected. Future inspections will be required to confirm the thinning rate at Pickering A, and to determine the need for future feeder pipe replacements. Pickering B feeder pipes have been found to be less affected by thinning than those at the Darlington and Pickering A generating stations.

Cracking of feeder pipes has been experienced at two CANDU plants located outside Ontario. At those plants, the affected sections of pipe were replaced and the units were returned to service. OPG has not experienced any feeder pipe cracking at any of its nuclear facilities, but is carrying out inspections during regularly planned outages. The scale of these inspections has been increased to address the concern that the risk of cracking may be increasing in OPG's units. OPG is also participating in research and development with other CANDU operators to better understand the degradation mechanisms.

The Pickering A reactors are unique among the CANDU fleet in that the reactor is contained within an air-filled concrete enclosure called the "calandria vault". The environment is potentially corrosive to carbon steel components contained within the calandria vault structure, particularly when the atmosphere is humid. Significant degradation of the carbon steel components occurred early in life. Maintenance was carried out during the 1980s and early 1990s to mitigate the degradation and repair some of the degraded components. Equipment was added to maintain a dry vault atmosphere and thereby significantly reduce the risk of corrosion. There is limited information to determine the extent to which mitigation efforts have been successful. Further inspections are being planned.

In 2004, inspections of Pickering A Unit 2 uncovered a single crack originating in the outer diameter of the steam generator tubing. This was the first crack observed in any of the Pickering A and B steam generator tubes and resulted in an increase in the scope of inspection for all Pickering A and B steam generators. Inspection of Pickering A Unit 4 in 2005 confirmed the presence of a single crack. Inspections of the other Pickering A and B units (including recent inspection of Pickering A Unit 1 in 2004 and Pickering B Units 5 and 6 in 2005) have not uncovered any further cracks. Operating units observed to have cracked tubes would likely require a shortened operating interval in the range of one year before inspection. Tubes which cannot be demonstrated to be fit for service can be removed from service; this may impact outage duration and costs.

Environmental Risk

OPG incurs substantial capital and operating costs to comply with environmental laws. The regulatory requirements relate to discharges to the environment; construction of or modifications to our facilities; the handling, use, storage, transportation, disposal and clean-up of hazardous substances and waste; and the decommissioning of generation facilities at the end of their useful lives.

OPG's Sustainable Development Policy commits OPG to meet all applicable legislative requirements and voluntary environmental commitments, integrate environmental factors into business planning and decision-making, and apply the precautionary principle in assessing risks to human health and the environment. This policy also commits OPG to maintain comprehensive EMSs at our generating facilities consistent with the ISO 14001 standard.

OPG monitors emissions into the air and water and regularly reports the results to various regulators, including the Ministry of Environment, Environment Canada and the Canadian Nuclear Safety Commission. The public also receives ongoing communications regarding OPG's environmental performance through community-based advisory groups, annual environmental reports, community newsletters, open houses and OPG's web site. OPG has developed and implemented internal monitoring, assessment and reporting programs to manage environmental risks such as air and water emissions, discharges, spills, radioactive emissions and radioactive wastes. OPG also continues to address historical land contamination through its voluntary land assessment and remediation program.

OPG's SO_2 and NO_x emissions are managed through the installation of specialized equipment such as scrubbers to reduce SO_2 emissions, low NO_x burners and selective catalytic reduction equipment to reduce NO_x emissions, and through the purchase of low sulphur fuel. OPG also utilizes a regulatory approved emissions trading program to manage emission levels within regulatory limits. The Province's coal replacement policy directs OPG to phase out the use of coal-fired generation during the period 2007 to 2009. In the interim, OPG will operate its coal-fired facilities in accordance with all regulatory requirements and will implement continuous improvement measures that are consistent with the remaining in-service requirements for these facilities.

OPG's emissions of greenhouse gases ("GHG") have been managed on a voluntary basis, primarily through improvements in energy efficiency and the purchase of GHG emission reduction credits. The Kyoto Protocol, to which Canada is a signatory, came into force on February 16, 2005. To meet Canada's international obligations under the Protocol, the federal government's Climate Change Plan includes the provision for regulations to be applied to Large Final Emitters ("LFE") of GHG, including OPG. The LFE regulations, if finalized as currently proposed, would require OPG to reduce the CO_2 intensity at each fossil facility in operation beyond 2008 by approximately 13.5 per cent relative to 2000 levels. Under the implementation timeline for the Government's coal replacement policy, Nanticoke generating station would be the only coal-fired facility running beyond 2008. As a result, the cost of achieving the proposed limit at Nanticoke through the use of emission reduction credits could be $60 million annually, assuming access to the $15/tonne carbon dioxide (CO_2) price assurance mechanism.

Changes to environmental laws or delays in implementing the current timetable of the Government's coal replacement policy could create compliance risks that may be addressed by the installation of additional equipment or control technologies, the purchase of additional emission reduction credits, or by constraining production from the fossil-fuelled fleet. In addition, a failure to comply with applicable environmental laws may result in enforcement actions, including the potential for orders or charges. Further, some of OPG's activities have the potential to cause contamination to land or water that may require remediation. The potential liability associated with any of these events could have a material adverse effect on the business.

Regulatory Risk

Through a regulation passed pursuant to the *Electricity Restructuring Act, 2004,* OPG receives regulated prices for its baseload hydroelectric and nuclear facilities from April 1, 2005. These prices are expected to remain in effect until at least March 31, 2008. Some time after March 31, 2008, the OEB is expected to establish new regulated prices. If there are changes to the fundamental assumptions on which these regulated prices were developed, the Province may amend these initial prices. Any such changes pose a risk that the return on equity factored into the existing prices could be reduced. Equally, to the extent that costs incremental to those included in the price determination process occur and no such amendments are made, these costs may be borne by OPG and not recovered through rates charged to future customers. These costs may be necessary to maintain the reliability and safety of OPG's regulated generating assets.

The regulation also directed OPG to establish variance accounts for costs incurred on or after April 1, 2005 that are associated with certain unforeseen circumstances, and to establish a deferral account for Pickering A return to service non-capital costs incurred on or after January 1, 2005. The accuracy and prudency of any variance account balances that OPG records as a regulatory asset or liability must be demonstrated by OPG to the OEB once it establishes new regulated prices expected after March 31, 2008. Regulatory risk arises given the possibility of the OEB not approving such costs. In the event that some of these costs are disallowed by the OEB at a future date, the amounts disallowed would be reflected in results of operations in the period that the OEB decision occurs.

Strategic Risk

OPG's operations are subject to government regulation and direction that may change. Matters that are subject to regulation include: structure of the electricity market, nuclear operations including regulation pursuant to the *Nuclear Safety and Control Act* (Canada), the *Nuclear Liability Act* (Canada) and the *Emergency Plans Act* (Ontario), nuclear waste management and decommissioning, water rentals, environmental matters including air emissions, and proxy tax payments. Because legal requirements can change and are subject to interpretation, OPG is unable to predict the impact of such changes on the Company and its operations.

Continuous Disclosure

Fourth Quarter

Net income for the three months ended December 31, 2005 was $160 million compared to net income of $34 million for the same period in 2004. Income before income taxes for the three months ended December 31, 2005 was $192 million compared to a loss of $80 million in the same period in 2004.

The details of the change in gross margin and other changes impacting fourth quarter income in 2005 compared to 2004, on a before-tax basis, are as follows:

(millions of dollars)	Three Months
Loss before income taxes for the three months ended December 31, 2004	**(80)**
Changes in gross margin	
Increase in electricity sales prices after Market Power Mitigation Agreement rebate and revenue limit rebate	230
Change in electricity generation by segment:	
Regulated – Nuclear	62
Regulated – Hydroelectric	(11)
Unregulated – Hydroelectric	11
Unregulated – Fossil-fuelled	(20)
Other changes in gross margin	(22)
	250
Decrease in Pickering A return to service OM&A expense due to deferral of non-capital costs in 2005 as a rate regulated asset	81
Increase in OM&A costs due to write-off of inventory as a result of not returning Pickering A generating station Units 2 and 3 to service	(35)
Increase in nuclear maintenance and repairs	(14)
Increase in pension and other post employment benefit costs	(21)
Increase in earnings on nuclear fixed asset removal and nuclear waste management funds	44
Other net changes	(33)
Increase in income before income taxes	**272**
Income before income taxes for the three months ended December 31, 2005	**192**

The increase in income before tax during the fourth quarter of 2005 was primarily attributable to a higher gross margin from electricity sales due to higher average sales prices compared to the same period in 2004. The increase in OPG's average sales prices in the fourth quarter of 2005 was due to higher Ontario spot market prices and the impact of the regulatory prices and related regulatory changes that took effect in 2005. Higher electricity generation in the fourth quarter of 2005 also contributed to the increase in gross margin. The increase in generation was primarily due to the return to service of Unit 1 of the Pickering A nuclear station in the fourth quarter of 2005, as well as strong performance from OPG's other nuclear generating stations.

The increase in earnings during the fourth quarter of 2005 compared to the same period last year was also due to lower OM&A expenses resulting from the deferral of non-capital costs related to the Pickering A return to service project in 2005, as required by a regulation pursuant to the *Electricity Restructuring Act, 2004,* and the completion of the Unit 1 return to service project. Amortization of the deferred OM&A amounts began during the fourth quarter of 2005 on the date of the return to service of Unit 1 in accordance with the regulation.

The improvement in earnings during the quarter was also due to higher income from the nuclear fixed asset removal and nuclear waste management funds due to a larger asset base and higher market returns compared to 2004.

The impact of these favourable changes on fourth quarter 2005 earnings was partially offset by higher OM&A expenses related to the write-off of additional inventory identified as excess as a result of the decision to not return Pickering A generating station Units 2 and 3 to service, higher nuclear maintenance and repairs expenditures, and higher pension and OPEB expenses.

After-tax earnings in the fourth quarter of 2005 were impacted by use of the taxes payable method, rather than the liability method, to account for income taxes relating to the rate regulated segments of its business upon inception of rate regulation in 2005. As a result of using this method, during the fourth quarter of 2005, OPG did not record a future tax expense for the rate regulated segments of $47 million, which would have been recorded had OPG accounted for income taxes for the regulated segments using the liability method.

In 2004, OPG's income tax expense was impacted by a reduction of $93 million in a valuation allowance for future income tax assets that had previously been established. This resulted in a reduction in the 2004 income tax provision, which did not recur in 2005.

Fourth Quarter Average Sales Prices

OPG's average sales prices by business segment, net of the revenue limit rebate, for the three months ended December 31, 2005, and net of the Market Power Mitigation Agreement for the three months ended December 31, 2004, are as follows:

	Three Months Ended December 31	
(¢/kWh)	**2005**	2004
Regulated – Nuclear[1]	**4.9**	4.0
Regulated – Hydroelectric[1]	**3.9**	4.0
Unregulated – Hydroelectric[2]	**5.5**	4.2
Unregulated – Fossil-fuelled[2]	**5.6**	4.1
OPG average price	**5.0**	4.0

1. During the period from April 1, 2005, electricity generation from stations in the Regulated – Nuclear segment received a fixed price of 4.95¢/kWh. During the same period, electricity generation 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.
2. During the period from April 1, 2005, 85 per cent of the electricity generation from unregulated stations, excluding the Lennox generating station and other contract volumes, was subject to a revenue limit based on an average price of 4.7¢/kWh.

Cash Flow from Operations

Cash flow provided by operating activities during the fourth quarter of 2005 was $446 million compared to $152 million during the same period in 2004. The favourable change in cash flow was primarily due to higher revenue and earnings compared to 2004 and lower rebate payments in 2005. The favourable changes were partly offset by higher pension contributions during the 2005 period.

Summary of Quarterly Results

The following tables set out certain unaudited interim consolidated financial statement information for each of the 12 most recent quarters ended December 31, 2005. The information has been derived from OPG's unaudited interim consolidated financial statements that, in management's opinion, have been prepared on a basis consistent with the audited consolidated financial statements. These operating results are not necessarily indicative of results for any future period.

			2005 Quarters Ended		
(millions of dollars)	**March 31**	**June 30**	**September 30**	**December 31**	**Total Year**
Revenue after Market Power Mitigation Agreement rebate and revenue limit rebate	**1,358**	**1,373**	**1,571**	**1,496**	**5,798**
(Loss) income before extraordinary item	**(38)**	**137**	**181**	**160**	**440**
(Loss) income before extraordinary item per share	**$(0.15)**	**$0.53**	**$0.71**	**$0.62**	**$1.72**
Net (loss) income	**(38)**	**63**	**181**	**160**	**366**
Net (loss) income per share	**$(0.15)**	**$0.25**	**$0.71**	**$0.62**	**$1.43**

			2004 Quarters Ended		
(millions of dollars)	March 31	June 30	September 30	December 31	Total Year
Revenue after Market Power Mitigation Agreement rebate	1,350	1,141	1,212	1,215	4,918
Net income (loss)	64	(41)	(15)	34	42
Net income (loss) per share	$0.25	$(0.16)	$(0.06)	$0.13	$0.16

			2003 Quarters Ended		
(millions of dollars)	March 31	June 30	September 30	December 31	Total Year
Revenue after Market Power Mitigation Agreement rebate	1,480	1,246	1,224	1,228	5,178
Net income (loss)	73	8	34	(606)	(491)
Net income (loss) per share	$0.28	$0.03	$0.13	$(2.36)	$(1.92)

Balance Sheets as at December 31 (millions of dollars)	**2005**	2004	2003
Total assets	**21,623**	19,830	19,511
Total long-term liabilities	**13,640**	13,366	13,043
Cash dividends declared per share	**–**	–	0.07
Common shares outstanding (millions)	**256.3**	256.3	256.3

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. The revenue limit and the Market Power Mitigation Agreement rebates, and OPG's hedging strategies significantly reduced the impact of seasonal price fluctuations on the results of operations. The quarterly performances are also impacted by the factors described in the Key Generation Performance Indicator section of the MD&A.

Since April 1, 2005, revenue has increased due to the introduction of regulated prices for OPG's baseload hydroelectric and nuclear facilities and other related regulatory changes.

Off-Balance Sheet Arrangements

Securitization

In October 2003, OPG completed a revolving securitization agreement with an independent trust. Under the securitization agreement, OPG sold an undivided co-ownership interest in certain current and future accounts receivable generated in the normal course of business. The amount of the co-ownership interest sold is removed from the consolidated balance sheet with each revolving securitization. OPG also retains an undivided co-ownership interest in the receivables sold to the trust. This retained interest is accounted for at cost on OPG's consolidated balance sheet. The independent trust is not controlled by OPG, nor is OPG the primary beneficiary. As such, the results of the trust are not consolidated. The securitization provides OPG with an opportunity to obtain an alternative source of cost effective funding. For the year ended December 31, 2005, the average all-in cost of funds was 3.1 per cent and the pre-tax charges on sales to the trust were $9 million. The initial net cash proceeds from this transaction of $300 million were used by OPG in the operation of its business. In December 2005, OPG extended the securitization agreement to August 2009. See Note 4 to the audited consolidated financial statements for more information.

Guarantees

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

Derivative Instruments

The majority of OPG's derivative instruments are treated as hedges, with gains or losses recognized upon settlement when the underlying transactions occur. OPG holds financial commodity derivatives primarily to hedge the commodity price exposure associated with changes in the price of electricity. OPG entered into forward-start interest rate swap agreements to hedge against the effect of future interest rate movements on 10-year fixed rate borrowing requirements for the Niagara tunnel project. Financial commodity derivative instruments are entered into with large and medium volume end-use consumers and intermediaries such as U.S. utilities, brokers, aggregators, traders and other power marketers and retailers. Foreign exchange derivative instruments entered into with major financial institutions are used to hedge the exposure to anticipated U.S. dollar denominated purchases.

When a derivative instrument ceases to exist 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. The deferred loss on electricity derivative instruments and interest rate hedges was $127 million as at December 31, 2005, compared to a deferred loss of $71 million on electricity derivative instruments as at December 31, 2004. See Note 12 to the audited consolidated financial statements for more information.

All contracts not designated as hedges are recorded as assets or liabilities at fair value with changes in fair value recorded in other revenue.

Related Party Transactions

Given that the Province owns all of the shares of OPG, related parties include the Province, the other successor entities of Ontario Hydro, including Hydro One Inc. ("Hydro One"), the IESO, and the OEFC. OPG also enters into related party transactions with its joint ventures.

The transactions between OPG and related parties are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

These transactions are summarized below:

(millions of dollars)	**Revenues 2005**	**Expenses 2005**	Revenues 2004	Expenses 2004
Hydro One				
Electricity sales	**40**	**–**	40	–
Services	**–**	**12**	–	12
Settlement Transactions	**–**	**27**	–	33
Province of Ontario				
GRC water rentals and land tax	**–**	**132**	–	152
Guarantee fee	**–**	**8**	–	8
Used Fuel Fund rate of return guarantee	**–**	**–**	–	14
Decommissioning Fund excess funding	**–**	**7**	–	–
Other	**–**	**–**	–	2
OEFC				
GRC and proxy property tax	**–**	**207**	–	214
Interest income on receivable	**–**	**(75)**	–	(101)
Interest expense on long-term notes	**–**	**211**	–	191
Capital tax	**–**	**51**	–	49
Income taxes	**–**	**192**	–	(80)
Indemnity fees	**–**	**5**	–	5
IESO				
Electricity sales	**6,517**	**329**	5,465	304
Market Power Mitigation Agreement rebate	**(412)**	**–**	(1,154)	–
Revenue limit rebate	**(739)**	**–**	–	–
Ancillary services	**68**	**–**	90	–
Other	**–**	**–**	1	1
	5,474	**1,106**	4,442	804

At December 31, 2005, accounts receivable included $14 million (2004 – $14 million) due from Hydro One and $324 million (2004 – $158 million) due from the IESO. Accounts payable and accrued charges at December 31, 2005 included $2 million (2004 – $3 million) due to Hydro One.

Corporate Governance

National Instrument 58-101, Disclosure of Corporate Governance Practices, has been implemented by Canadian securities regulatory authorities to provide greater transparency for the marketplace regarding issuers' corporate governance practices. Information with respect to OPG's Board of Directors is as follows:

Board of Directors and Directorships

OPG's Board of Directors is made up of individuals with substantial expertise in managing and restructuring large businesses, managing and operating nuclear stations, managing capital intensive companies, and overseeing regulatory, government and public relations. The Board exercises its independent supervision over management as follows: with the exception of the CEO, all members of the Board are independent of the Company; meetings of the Board are held at least six times a year; a formal Charter for the Board, and for each Board Committee has been adopted; each Board Committee is chaired by an independent director; and a portion of each Board and Committee meeting is reserved for directors to meet without management present.

The following are the directors of OPG as at December 31, 2005:

Name	Principal occupation	Other directorship in any other reporting issuer (or equivalent in a foreign jurisdiction)
Hon. Jake Epp	Chairman, Ontario Power Generation Inc. Board of Directors	QHR Technologies Inc.
Donald Hintz	Retired President of Entergy Corporation	Entergy Corporation
Dr. Gary Kugler	Retired Senior Vice President, Nuclear Products and Services, Atomic Energy of Canada Limited	None
George Lewis	Chairman and Chief Executive Officer of RBC Asset Management Inc.	None
David MacMillan	Non-executive director of Killingholme Power	None
Corbin McNeill	Retired Chairman and Co-Chief Executive Officer of Exelon Corporation	Owens Illinois, Inc. Portland General Electric Company
Peggy Mulligan	Chief Financial Officer, Linamar Corporation	None
Ian Ross	Chairman, GrowthWorks Canadian Fund Ltd.	World Heart Corporation PetValu Canada Inc. GrowthWorks Canadian Fund Ltd.
Marie Rounding	Former President and Chief Executive Officer of the Canadian Gas Association	None
William Sheffield	Corporate Director	Velan Inc. Royal Group Technologies Limited
David Unruh	Corporate Director	Westcoast Energy Inc. Union Gas Limited Pacific Northern Gas Ltd. Corriente Resources Inc.
Jim Hankinson*	President and CEO, Ontario Power Generation Inc.	Maple Leaf Foods Inc. CAE Inc. Entertainment One Income Fund

* All directors listed are independent within the meaning of section 1.4 of Multilateral Instrument 52-110, Audit Committees (MI 52-110) except for Jim Hankinson who is the President and CEO of the Company.

Orientation and Continuing Education

In 2005, the Board established an orientation program for new Directors when they join the OPG Board. New directors participate in a range of orientation initiatives:

- Directors receive an overview of relevant documentation arising from a new director's election to the Board,
- Directors are provided a Director's Handbook, which provides an overview of the Board's constitution and governance practices, including Shareholder Agreements, Board and Committee Charters, Director roles and responsibilities, Board and Committee chair position descriptions, Board approved corporate policies and Code of Conduct, Director and Officer indemnities and insurance, Board and Committee evaluations, and recent Board activity,
- Directors attend a comprehensive introductory briefing session on OPG's operations and business, and
- Plant tours are provided of OPG generating facilities.

The Board supports the continuing education of directors, in both the business of OPG and their duties as directors, in a number of ways:

- Special presentations are made to the Board or a Committee on specific or unique aspects of OPG's operations, for example OPG hedging activities and controls, and nuclear waste management,
- Approximately every other Board meeting is preceded by a Board education session. Suggestions for director education sessions are submitted to the Chair of the Governance and Nominating Committee,
- Plant tours to major facilities are arranged in conjunction with director orientation sessions as well as the holding of Board meetings at OPG facilities,
- OPG sponsors director attendance at the Institute of Corporate Directors/Rotman Business School Director College, or equivalent, and
- OPG also provides support to directors for attendance at conferences related to OPG's business or continuing education sessions related to their responsibilities as directors.

Ethical Business Conduct

OPG has a policy for ethical business behaviour and a Code of Business Conduct, which is approved by the Board. The Audit and Risk Committee Charter expressly includes regular reporting by Management on the Code of Business Conduct, including reports on substantiated cases of fraud and the disposition of such cases including disciplinary action. The Audit and Risk Committee also receives an annual report on the Code of Business Conduct in order to satisfy itself that appropriate codes of conduct and compliance programs are in place and are being enforced and remedial action is being taken. A copy of OPG's Code of Business Conduct has been filed with the OSC. The Audit and Risk Committee has also established procedures for the receipt, retention and treatment of complaints received pertaining to internal accounting controls or auditing matters and the confidential anonymous submission by employees concerning such matters. The Audit and Risk Committee also received a report on the communication to employees of the new procedures.

The Board has accepted a recommendation from the Governance and Nominating Committee for the implementation of an annual process of written disclosure by directors of information in order to: (i) identify potential conflicts of interest for the purposes of complying with the Ontario Business Corporations Act, (ii) validate their independence and financial literacy for the purposes of complying with securities regulations related to Boards and Audit Committees, and (iii) satisfy other disclosures and filings.

Nomination of Directors

In the spring of 2004, the Board established a Search Committee and hired an independent search firm to assist in the identification of skills, attributes and business experience that would be appropriate for the OPG Board of Directors, given the nature, complexity and risk of OPG's business. Upon approval by the Board of the appropriate skills and competencies profile, the search firm recommended candidates to be interviewed by the Search Committee. The Search Committee made its recommendations to the Board, and a slate of proposed directors was submitted to the Shareholder in the fall of 2004. The Search Committee was disbanded and directors were elected to the Board by the Shareholder in September and October 2004, and February 2005.

The Board recently established a permanent Governance and Nominating Committee, and among its responsibilities are to: (i) develop and maintain list of optimum skills which the Board should collectively possess, (ii) recommend a process to identify director candidates, (iii) recommend selection criteria, (iv) identify director candidates to the Board and (v) recommend to the Board the candidates to stand for election. The Board submits recommended candidates to the Shareholder. Nominations of directors by the Shareholder are also reviewed by the Governance and Nominating Committee.

In December of 2005, the Shareholder appointed an additional director to the OPG Board. The Board now consists of 12 directors.

Compensation

Director Compensation

In the spring of 2005, the Compensation and Human Resources Committee of the Board retained an independent advisor to benchmark OPG director compensation against companies similar in size, business complexity and risk profile. The Compensation and Human Resources Committee submitted its recommendations for director compensation to the Board for approval. The Board Chair subsequently informed the Shareholder.

The recently established Governance and Nominating Committee has assumed responsibility for monitoring and reviewing at least annually the level and nature of compensation of directors to ensure that it is both appropriate to the responsibilities and risks assumed, and competitive with other comparable organizations.

CEO Compensation

In the spring of 2005, the Compensation and Human Resources Committee of the Board retained an independent advisor to benchmark an appropriate compensation package for the recruitment of the President and CEO, given the nature, complexity and risk profile of OPG's business. The Compensation and Human Resources Committee submitted its recommendation to the Board for approval. The Board Chair subsequently informed the Shareholder.

The Compensation and Human Resources Committee of the Board oversees, on behalf of the Board, the setting of the CEO's annual goals and objectives and the annual review of CEO performance, and makes recommendations to the Board with respect to CEO compensation. The Compensation and Human Resources Committee seeks input from an independent advisor with regard to monitoring and benchmarking compensation developments.

Board Committees

The Board has established six committees to focus on areas critical to the Company:

Audit and Risk Committee

The Committee is responsible for reviewing the Company's regulatory filings including financial statements, MD&A, and press releases prior to their disclosures to the public. The Committee is also responsible for overseeing the internal audit function, the work of external auditors including their nomination and compensation, that the Company has adequate controls in the financial reporting process and the risk management process, and is in compliance with regulatory and internal policies. The Committee is also responsible for overseeing OPG's policy on ethical behaviour and the Code of Business Conduct, including reports on compliance programs, substantiated cases of fraud and the disposition of such cases including disciplinary action.

Governance and Nominating Committee

The Committee develops governance principles for OPG that are consistent with high standards of corporate governance and reviewing and assessing on an ongoing basis OPG's system of corporate governance with a view to maintaining these high standards. The Committee identifies and recommends candidates for election or appointment to the Board to be put before the Shareholder in the event of a vacancy on the Board. Finally, the Committee reviews and recommends OPG's processes for director orientation, assessment, and compensation.

Nuclear Operations Committee

This Committee is responsible for oversight of safe and efficient operations of OPG's nuclear business, regulatory compliance of OPG's nuclear facilities, review of reports from independent oversight of OPG's nuclear operations, reviews of OPG nuclear management and organization matters, security of OPG's nuclear facilities and substances, and oversight of OPG's nuclear waste and decommissioning liabilities and management.

Investment Funds Oversight Committee

This Committee assists the Board in fulfilling its responsibilities for the OPG Pension Fund and the Used Fuel Fund and Decommissioning Fund. The Committee provides oversight of the investment of assets, investment-related liabilities and the management of any surplus (deficit) of the funds. Specifically the Committee: reviews the investment policies, risks and the asset mix; approves annual performance objectives for the investment portfolios; and monitors the performance of the funds.

Compensation and Human Resources Committee

This Committee focuses on human resources related areas including compensation practices, CEO objectives and compensation, disclosure on compensation and human resources matters, leadership talent review including succession planning, human resources policies related to employee complaints, diversity and pay equity, organizational design, labour relations, pension plans and policies, and Board compensation, education and evaluation programs.

Major Projects Committee

This Committee assists the Board in providing oversight of major non-nuclear electricity supply projects, including project development, contracting, financing, and construction monitoring.

Assessments

In 2005, the Board established an annual evaluation process for the Board and Board Committees. The annual Committee Evaluation, consisting of the completion of confidential questionnaires regarding Committee Charters and operations, was launched by the Governance and Nominating Committee in November 2005. The results and recommendations for enhancing oversight will be reported to the Board by the Chair of the Governance and Nominating Committee early in 2006. The Board will be undertaking the assessment of the Board and its Charter in 2006.

Audit and Risk Committee Information

Multilateral Instrument 52-110, Audit Committees (the "Instrument") has been implemented by Canadian securities regulatory authorities to encourage reporting issuers to establish and maintain strong, effective and independent audit committees, which enhance the quality of financial disclosure and ultimately foster increased investor confidence in Canada's capital markets. Information on OPG's Audit and Risk Committee, which includes the text of the Audit and Risk Committee Charter, updated during 2005, is as follows:

Audit and Risk Committee Charter

Purpose

The purpose of the Audit and Risk Committee (the "Committee") is to assist the Board in fulfilling its oversight responsibilities by reviewing, advising and making recommendations to the Board on:

- The integrity, quality and transparency of the Company's financial information,
- The adequacy of the financial reporting process,
- The systems of internal controls and risk management, and the Company's related principles, policies and procedures which Management have established,
- The performance of the Company's internal audit function and the external auditors,
- The external auditors' qualifications and independence,
- The Company's compliance with related legal and regulatory requirements and internal policies, and
- The promotion of a culture of ethical business conduct and compliance with OPG's Code of Business Conduct.

The function of the Audit and Risk Committee is oversight. Management is responsible for the preparation, presentation and integrity of the consolidated financial statements of the Company. Management of the Company is responsible for maintaining appropriate accounting and financial reporting principles and policy and internal controls and procedures that provide for compliance with accounting standards and applicable laws and regulations.

Organization

Members

The Audit and Risk Committee shall consist of three or more independent Directors appointed by the Board of Directors, none of whom shall be employees of the Company or any of the Company's affiliates. A majority of the members of the Committee, but not less than two, will constitute a quorum.

As a venture issuer, OPG is exempt from the statutory requirements of Multilateral Instrument 52-110 requiring members of Audit Committees to be independent. However, OPG considers such independence to be "best practice" and, therefore, each of the members of the Audit and Risk Committee shall satisfy the applicable independence and financial literacy requirements of the laws and regulations governing the Company.

The Board of Directors shall designate one member of the Audit and Risk Committee as the Committee Chair. Members of the Audit and Risk Committee shall serve at the pleasure of the Board of Directors for such term or terms as the Board of Directors may determine. The Board of Directors shall confirm that each member of the Audit and Risk Committee is financially literate as such qualification is interpreted by the Board of Directors in its business judgment and in compliance with Multilateral Instrument 52-110 and its Companion Policy.

Meetings

The Committee will meet at least quarterly or more frequently as circumstances require and at any time at the request of a member. The Committee will meet regularly and at least annually with the external auditors, the internal auditors and Management in separate sessions to discuss any matters that the Committee believes should be discussed and to provide a forum for any relevant issues to be raised.

Reports

The Committee will report its activities and actions to the Board of Directors with recommendations, as the Committee deems appropriate.

The Committee will provide for inclusion in the Company's financial information or regulatory filings any report from the Audit and Risk Committee required by applicable laws and regulations and stating among other things whether the Audit and Risk Committee has:

- Reviewed and discussed the audited consolidated financial statements with Management,
- Discussed pertinent matters with the internal and external auditors,
- Received disclosures from the external auditors regarding the auditors' independence and discussed with the auditors their independence, and
- Recommended to the Board of Directors that the audited consolidated financial statements be included in the Company's Annual Report.

Authority
While the Audit and Risk Committee has the responsibilities and powers set forth in this Charter, it is not the duty of the Audit and Risk Committee to plan or conduct audits or risk assessments, or to determine that the Company's consolidated financial statements and disclosures are complete and accurate and are in accordance with generally accepted accounting principles and applicable rules and regulations. These are the responsibility of Management and the external auditor.

In carrying out its oversight responsibilities, the Audit and Risk Committee and the Board will necessarily rely on the expertise, knowledge and integrity of the Company's Management, and internal and external auditors.

The Audit and Risk Committee shall have the authority to set and pay the compensation for any advisors employed by the Committee.

The Audit and Risk Committee shall have the authority to communicate directly with the internal and external auditors.

Delegation of Authority

The Committee may delegate to any employee of OPG or a sub-committee the authority to: (i) execute or carry out any decision of the Committee; and/or (ii) exercise any right, power or function of the Committee on such terms and conditions and within such limits as the Committee may establish, except that the Committee may not delegate its oversight responsibilities.

Access to Management and Outside Advisors

The Audit and Risk Committee shall have unrestricted access to members of Management and relevant information. The Audit and Risk Committee may retain independent counsel, accountants or other advisors to assist it in the conduct of any investigation, as it determines necessary to carry out its duties.

Committee Responsibilities and Duties
The Committee shall:

General

- Conduct or authorize investigations into any matters within the Committee's scope of responsibilities,
- Review and recommend approval to the Board, the appointment or replacement of the CFO and the Chief Risk Officer (CRO), and
- Review and approve the Company's hiring policies regarding partners, employees and former partners and employees of the present and former external auditor of the Company.

Risk Management and Internal Controls

- Review and evaluate the Company's policies and processes for assessing significant risks or exposures and the steps Management has taken to monitor and control such risks to the Company, including the organizational structure and the adequacy of resources,
- Consider and review with the CRO and Management the critical risks to the Company, the potential impact of such risks, and related mitigation,
- Ascertain whether the Company has an effective process for determining risks and exposure from actual and potential litigation and claims relating to non-compliance with laws and regulations,
- Review with Management, reports demonstrating compliance with risk management policies,
- Review with the Company's General Counsel and others any legal, tax, or regulatory matters that may have a material impact on Company operations and the financial statements, including, but not limited to, violations of securities law or breaches of fiduciary duty,
- Review with Management, internal audit, and the external auditors, the scope of review of internal control over financial reporting, significant findings, recommendations and Management's responses for implementation of actions to correct weaknesses in internal controls,
- Review disclosures made by the CEO and CFO during the certification process regarding significant deficiencies in the design or operation of internal controls or any fraud that involves Management or other employees who have a significant role in the Company's internal controls, and
- Review the expenses of the Chairman, CEO and the CEO's direct reports on a semi-annual basis, and of any other senior officers and employees the Committee considers appropriate.

Internal Audit

- Evaluate the internal audit process and define expectations in establishing the annual internal audit plan and the focus on risk, including the organizational structure and the adequacy of resources,
- Approve the Charter of the internal audit function annually,
- Evaluate the audit scope and role of internal audit, and
- Consider and review with the CRO and Management:
  - Significant findings and Management's response including the timetable for implementation of Management Actions to correct weaknesses,
  - Any difficulties encountered in the course of their audit (such as restrictions on the scope of their work or access to information),
  - Any changes required in the planned scope of the audit plan, and
  - The internal audit budget.

External Auditor

- Recommend to the Board of Directors the external auditor to be nominated for the purpose of preparing or issuing an auditor's report or performing other audit, review or attest services for the Company, and the compensation of the external auditor,
- Oversee the work of the external auditor engaged for the purpose of preparing or issuing an auditor's report or performing other audit, review or attest services for the Company, including the resolution of disagreements between Management and the external auditor regarding financial reporting,
- Review the independence and qualifications of the external auditor,
- At least annually, obtain and review a report by the external auditor describing the auditing firm's internal quality control procedures, any material issues raised by the most recent internal quality control review or peer review of the auditing firm or by any inquiry or investigation by governmental or professional authorities within the preceding five years respecting one or more independent audits carried out by the external auditor and any steps taken to deal with any such issues and all relationships between the external auditors and the Company,
- Review the scope and approach of the annual audit plan with the external auditors,
- Discuss with the external auditor the quality and acceptability of the Company's accounting principles including all critical accounting policies and practices used, any alternative treatments that have been discussed with Management as well as any other material communications with Management,
- Assess the external auditor's process for identifying and responding to key audit and internal control risks,
- Ensure the rotation of the lead audit partner every five years and other audit partners every seven years, and consider regular rotation of the audit firm,
- Evaluate the performance of the external auditor annually and present its findings to the Board of Directors,
- Determine which non-audit services the external auditor is prohibited by law or regulation, or as determined by the Audit and Risk Committee, from providing and pre-approve all services provided by the external auditors. The Committee may delegate such pre-approval authority to a member of the Committee. The decision of any Committee member to whom pre-approval authority is delegated must be presented to the full Audit and Risk Committee at its next scheduled meeting, and
- Review and approve all related party transactions.

Financial Reporting

- Review with Management and the external auditors the Company's interim financial information and disclosures under MD&A and earnings press release, prior to filing,
- Satisfy itself that adequate procedures are in place for the review of the Company's public disclosure of financial information extracted or derived from the Company's consolidated financial statements, other than the public disclosure referred to above, and periodically assess the adequacy of those procedures,
- Review with Management and the external auditors, at the completion of the annual audit:
  - The Company's annual financial statements, MD&A, related footnotes and any documentation required by the Securities Act to be prepared and filed by the Company or that the Company otherwise files with the OSC,
  - The external auditors' audit of the consolidated financial statements and their report,
  - Any significant changes required in the external auditors' audit plan,
  - Any difficulties or disputes with Management encountered during the audit,
  - The Company's accounting principles, and
  - Other matters related to conduct, which should be communicated to the Committee under generally accepted auditing standards.
- Review significant accounting and reporting issues and understand their impact on the consolidated financial statements. These include complex or unusual transactions and highly judgmental areas; major issues regarding accounting principles and financial presentations, including significant changes in the Company's selection or application of accounting principals; and the effect of regulatory and accounting initiatives, as well as off-balance sheet arrangements, on the consolidated financial statements of the Company,
- Review analysis prepared by Management and/or the external auditor detailing financial reporting issues and judgments made in connection with the preparation of financial information, including analysis of the effects of alternative generally accepted accounting principles methods, and
- Advise Management, based upon the Audit and Risk Committee's review and discussion, whether anything has come to the Committee's attention that causes it to believe that the consolidated financial statements contain an untrue statement of material fact or omit to state a necessary material fact.

Compliance with Code of Business Conduct

- Review the administration of and compliance with the Company's Code of Business Conduct to ensure that appropriate codes of conduct and compliance programs are in place, are being enforced and remedial action is being taken, as well as the process for communicating the Code of Business Conduct to Company personnel, and
- Monitor through regular updates from Management regarding compliance matters.

Treatment of Complaints

- Establish procedures for the receipt, recording and treatment of complaints received by the Company regarding accounting, internal accounting controls, or auditing matters, and
- Establish procedures for the confidential and anonymous submission by employees of concerns regarding accounting or auditing matters of the Company.

Annual Review and Assessment

The Committee shall conduct an annual review and assessment of its performance, including a review of its compliance with this Charter, in accordance with the evaluation process approved by the Board.

The Committee shall also review and assess the adequacy of this Charter on an annual basis taking into account all legislative and regulatory requirements applicable to the Committee as well as any best practice guidelines recommended by regulators with whom OPG has a reporting relationship, and if appropriate, shall recommend changes to the Board.

Composition of the Audit and Risk Committee

Each Audit and Risk Committee member named below is independent and financially literate.

Gary Kugler

Dr. Gary Kugler is the retired Senior Vice President, Nuclear Products and Services of Atomic Energy of Canada, Limited (AECL), where he was responsible for all of AECL's commercial operations, including nuclear power plant sales and services world-wide. During his 34 years with AECL, he also held various technical, project management, and business development positions. Prior to joining AECL, he served as a pilot in the Canadian air force. Dr. Kugler holds a Bachelor of Science degree in honours physics and a Ph.D. in nuclear physics from McMaster University.

M. George Lewis – Chair

George Lewis is Chairman and Chief Executive Officer of RBC Asset Management Inc., Mr. Lewis is also Executive Vice President, Wealth Management for the Personal and Business Canada division of RBC FG, Canada's largest bank. Formerly he was Managing Director, Head of Institutional Equity Sales, Trading and Research with RBC Capital Markets and was Canada's top-rated analyst for three consecutive years. He has extensive experience in the investment industry and has a Master of Business Administration degree with distinction from Harvard University, a Bachelor of Commerce degree with high distinction from Trinity College at the University of Toronto and is a chartered financial analyst and chartered accountant.

C. Ian Ross

Ian Ross served at the Richard Ivey School of Business at the University of Western Ontario from 1997 to September 2003. Most recently he held the position of Senior Director, Administration in the Dean's Office, and was also Executive in Residence for the School's Institute for Entrepreneurship, Innovation and Growth. He has served as Governor and President and CEO of Ortech Corporation; Chairman, President and CEO of Provincial Papers Inc.; and President and CEO of Paperbound Industries Corp. Mr. Ross currently serves as a Director for a number of corporations including World Heart Corporation, GrowthWorks Canadian Fund Ltd., PetValu Canada Inc., Comcare Health Services and eJust Systems (formerly Praeda Managements Systems). He is also a member of the Law Society of Upper Canada.

David G. Unruh

David Unruh is a lawyer currently serving as a director of Westcoast Energy Inc. and Union Gas Limited, both Duke Energy companies. Mr. Unruh is also a director of Export Development Canada, Pacific Northern Gas Ltd., Corriente Resources Inc., The Wawanesa Mutual Insurance Company, The Wawanesa General Insurance Company, The Wawanesa Life Insurance Company, and RAV Project Management Company. Prior to this, Mr. Unruh served as Vice Chairman of Westcoast Energy Inc. and Union Gas Limited, before that as Senior Vice President and General Counsel for Houston-based Duke Energy Gas Transmission and, before that as Senior Vice President, Law and Corporate Secretary of Westcoast Energy Inc. Mr. Unruh practiced corporate and commercial law in Winnipeg, Manitoba before joining Westcoast Energy Inc. in Vancouver, British Columbia in 1993.

Audit and Risk Committee Oversight

There have been no recommendations of our Audit and Risk Committee to nominate or compensate an external auditor which have not been adopted by our Board of Directors.

Reliance on Certain Exemptions

There has been reliance upon the exemption in Section 6.1 of Multilateral Instrument 52-110 Audit Committees ("Instrument 52-110") as it relates to Section 5, *Reporting Obligations*. OPG has, however, in accordance with Section 6.2 of Instrument 52-110, provided the disclosure required by Form 52-110F2.

Pre-Approval Policies and Procedures

In accordance with the provisions of its mandate, the Audit and Risk Committee ratifies all non-audit services to be provided to the Company by its external auditor.

External Auditor Service Fees

The following fees were billed by Ernst & Young LLP:

(thousands of dollars)	**2005**	2004
Audit Fees	**1,227**	1,267
Audit-Related Fees	**277**	995
Tax Fees and Other	**320**	122

Audit Fees
These fees included the audit of OPG's consolidated financial statements, quarterly reviews of the financial statements, pension fund audit, and the audits of the financial statements of certain subsidiaries.

Audit-Related Fees
These fees included work with respect to internal controls, accounting assistance, French translation of consolidated financial statements and MD&A, and special audits and reviews. During 2005, OPG has employed the services of other professional advisers, particularly in the areas of internal controls and accounting assistance.

Tax Fees and Other
These fees included tax services related to a U.S. Federal tax review and other income tax matters.

Internal Controls over Financial Reporting and Disclosure Controls

OPG continues to enhance the process by which it designs and tests the operating effectiveness of internal controls over financial reporting. Concurrently with this process, OPG has evaluated disclosure controls and procedures and concluded that these controls and procedures operated effectively at the end of the period covered by the annual filing. Concurrent with the filing of the MD&A, OPG has provided the CEO and CFO certification required by Multilateral Instrument 52-109, Certification of Disclosure in Issuers' Interim and Annual Filings ("Instrument 52-109"), around the design and operating effectiveness of disclosure controls and procedures, effective December 31, 2005.

OPG is working toward providing support for the full certification detailed in Instrument 52-109 by continuing its project to document, test and evaluate internal controls over financial reporting and to design remedies where deficiencies are noted. The full certification for reporting issuers around the responsibility for establishing and maintaining internal controls over financial reporting, the design of those controls, and the disclosure in the MD&A of material changes in those controls, is effective December 31, 2006. The project team continues to work with process owners to address all findings identified during the 2005 testing cycle, which incorporated significant financial processes, disclosure controls, and entity level controls.

OPG is also working to implement a program designed to meet the full certification requirements for non-venture issuers identified in Instrument 52-109. These requirements, which are effective December 31, 2006, add disclosure to the Audit and Risk Committee of significant and material weakness and disclosure of fraud that involves individuals who have a significant role in internal controls over financial reporting. In addition, OPG is monitoring the management and audit report requirements for non-venture issuers identified in the proposed Multilateral Instrument 52-111, Reporting on Internal Control over Financial Reporting.

Supplemental Earnings Measures

In addition to providing net income in accordance with Canadian generally accepted accounting principles, OPG's MD&A, consolidated financial statements for the year ended December 31, 2005 and 2004 and the notes thereto, present non-GAAP financial measures. These financial measures do not have standard definitions prescribed by Canadian generally accepted accounting principles ("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 Market Power Mitigation Agreement and revenue limit rebates and fuel expense.

(2) Restructuring expenses are defined as costs incurred to implement a fundamental and material change to the operating and/or management structures of the Company. Restructuring expenses may include severance costs, termination benefits and related pension and OPEB expenses, professional fees, travel costs and other incremental costs directly associated with the restructuring activities.

(3) Earnings is defined as net income.

For further information, please contact:

Investor Relations	416-592-6700 1-866-592-6700 investor.relations@opg.com
Media Relations	416-592-4008 1-877-592-4008 www.opg.com
Other	www.sedar.com

Statement of Management's Responsibility for Financial Information

Ontario Power Generation Inc.'s ("OPG") management is responsible for presentation and preparation of the annual consolidated financial statements and Management's Discussion and Analysis ("MD&A").

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and the requirements of the Ontario Securities Commission ("OSC"), as applicable. The MD&A has been prepared in accordance with the requirements of securities regulators, including National Instrument 51-102 of the Canadian Securities Administrators and its related published requirements.

The consolidated financial statements and information in the MD&A necessarily include amounts based on informed judgments and estimates of the expected effects of current events and transactions with appropriate consideration to materiality. Something is considered material if it is reasonably expected to have a significant impact on the Company's earnings, cash flow, value of an asset or liability, or reputation. In addition, in preparing the financial information we must interpret the requirements described above, make determinations as to the relevancy of information to be included, and make estimates and assumptions that affect reported information. The MD&A also includes information regarding the impact of current transactions and events, sources of liquidity and capital resources, operating trends, risks and uncertainties. Actual results in the future may differ materially from our present assessment of this information because future events and circumstances may not occur as expected.

In meeting our responsibility for the reliability of financial information, we maintain and rely on a comprehensive system of internal control and internal audit, including organizational and procedural controls and internal controls over financial reporting. Our system of internal controls includes written communication of our policies and procedures governing corporate conduct and risk management; comprehensive business planning; effective segregation of duties; delegation of authority and personal accountability; careful selection and training of personnel; and sound and conservative accounting policies, which we regularly update. This structure ensures appropriate internal control over transactions, assets and records. We also regularly audit internal controls. These controls and audits are designed to provide us with reasonable assurance that the financial records are reliable for preparing financial statements and other financial information, assets are safeguarded against unauthorized use or disposition, liabilities are recognized, and we are in compliance with all regulatory requirements.

We, as OPG's Chief Executive Officer and Chief Financial Officer, will certify OPG's annual disclosure document filed with the OSC, which includes attesting to the effectiveness of OPG's disclosure controls and procedures, as required by Multilateral Instrument 52-109.

The Board of Directors, based on recommendations from its Audit and Risk Committee, reviews and approves the consolidated financial statements and the MD&A, and oversees management's responsibilities for the presentation and preparation of financial information, maintenance of appropriate internal controls, management and control of major risk areas and assessment of significant and related party transactions.

The consolidated financial statements have been audited by Ernst & Young LLP, independent external auditors appointed by the Board of Directors. The Auditors' Report outlines the auditors' responsibilities and the scope of their examination and their opinion on OPG's consolidated financial statements. The independent external auditors, as confirmed by the Audit and Risk Committee, had direct and full access to the Audit and Risk Committee, with and without the presence of management, to discuss their audit and their findings therefrom, as to the integrity of OPG's financial reporting and the effectiveness of the system of internal controls.

Jim Hankinson
President and Chief Executive Officer

Donn W.J. Hanbidge
Chief Financial Officer

February 7, 2006

Auditors' Report

To the Shareholder of Ontario Power Generation Inc.

We have audited the consolidated balance sheets of Ontario Power Generation Inc. as at December 31, 2005 and 2004 and the consolidated statements of income, retained earnings (deficit) and cash flows for the years then ended. These consolidated financial statements are the responsibility of Ontario Power Generation Inc.'s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of Ontario Power Generation Inc. as at December 31, 2005 and 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Ernst & Young LLP
Chartered Accountants

Toronto, Canada
February 7, 2006

Consolidated Statements of Income

Years Ended December 31 (millions of dollars except where noted)	2005	2004
Revenue		
Revenue before Market Power Mitigation Agreement and revenue limit rebates	**6,949**	6,072
Market Power Mitigation Agreement rebate (note 17)	**(412)**	(1,154)
Revenue limit rebate (note 18)	**(739)**	–
	5,798	4,918
Fuel expense	**1,297**	1,153
Gross margin	**4,501**	3,765
Expenses		
Operations, maintenance and administration	**2,516**	2,594
Depreciation and amortization (note 5)	**753**	765
Accretion on fixed asset removal and nuclear waste management liabilities	**476**	453
Earnings on nuclear fixed asset removal and nuclear waste management funds	**(381)**	(313)
Property and capital taxes	**107**	103
Restructuring	**10**	20
	3,481	3,622
Income before the following:	**1,020**	143
Impairment of long-lived assets (note 5)	**265**	–
Other income	**–**	(8)
Income before interest, income taxes and extraordinary item	**755**	151
Net interest expense	**197**	189
Income (loss) before income taxes and extraordinary item	**558**	(38)
Income tax expense (recovery)		
Current	**80**	21
Future (note 10)	**38**	(101)
	118	(80)
Income before extraordinary item	**440**	42
Extraordinary item (note 10)	**74**	–
Net income	**366**	42
Basic and diluted income per common share before extraordinary item (dollars)	**1.72**	0.16
Basic and diluted income per common share (dollars)	**1.43**	0.16
Common shares outstanding (millions)	**256.3**	256.3

See accompanying notes to the consolidated financial statements

Consolidated Statements of Retained Earnings (Deficit)

As at December 31 (millions of dollars)	2005	2004
Deficit, beginning of year	**(105)**	(147)
Net income	**366**	42
Retained earnings (deficit), end of year	**261**	(105)

See accompanying notes to the consolidated financial statements

Consolidated Statements of Cash Flows

Years Ended December 31 (millions of dollars)	**2005**	2004
Operating activities		
Net income	**366**	42
Adjust for non-cash items:		
Depreciation and amortization	**753**	765
Accretion on fixed asset removal and nuclear waste management liabilities	**476**	453
Earnings on nuclear fixed asset removal and nuclear waste management funds	**(381)**	(313)
Pension cost	**115**	92
Other post employment benefits and supplementary pension plans	**181**	157
Future income taxes	**38**	(101)
Transition rate option contracts	**(36)**	(52)
Provision for restructuring	**10**	20
Mark-to-market adjustment on energy contracts	**18**	5
Provision for used nuclear fuel	**28**	28
Impairment of long-lived assets	**265**	–
Excess inventory write-off	**57**	–
Extraordinary item	**74**	–
Regulatory assets and liabilities	**7**	–
Other	**22**	26
	1,993	1,122
Contributions to nuclear fixed asset removal and nuclear waste management funds	**(454)**	(454)
Expenditures on fixed asset removal and nuclear waste management	**(90)**	(71)
Reimbursement of expenditures on nuclear fixed asset removal and nuclear waste management	**23**	19
Contributions to pension fund	**(254)**	(154)
Expenditures on other post employment benefits and supplementary pension plans	**(65)**	(60)
Expenditures on restructuring (note 15)	**(18)**	(51)
Net changes to other long-term assets and liabilities	**(87)**	(26)
Changes in non-cash working capital balances (note 25)	**153**	(99)
Cash flow provided by operating activities	**1,201**	226
Investing activities		
Investment in regulatory assets (note 6)	**(265)**	–
Investment in fixed assets	**(498)**	(561)
Proceeds on sale of other fixed assets	**3**	18
Cash flow used in investing activities	**(760)**	(543)
Financing activities		
Issuance of long-term debt (note 8)	**495**	13
Repayment of long-term debt (note 8)	**(4)**	(6)
Net increase (decrease) in short-term notes (note 7)	**(26)**	26
Cash flow provided by financing activities	**465**	33
Net increase (decrease) in cash and cash equivalents	**906**	(284)
Cash and cash equivalents, beginning of year	**2**	286
Cash and cash equivalents, end of year	**908**	2

See accompanying notes to the consolidated financial statements

Consolidated Balance Sheets

As at December 31 (millions of dollars)	**2005**	2004
Assets		
Current assets		
Cash and cash equivalents	**908**	2
Accounts receivable (note 4)	**538**	346
Future income taxes (note 10)	**18**	44
Fuel inventory	**581**	569
Materials and supplies	**115**	92
	2,160	1,053
Fixed assets (note 5)		
Property, plant and equipment	**15,172**	15,114
Less: accumulated depreciation	**3,760**	3,174
	11,412	11,940
Other long-term assets		
Deferred pension asset (note 11)	**663**	524
Nuclear fixed asset removal and nuclear waste management funds (note 9)	**6,788**	5,976
Long-term materials and supplies	**273**	281
Regulatory assets (note 6)	**266**	–
Long-term accounts receivable and other assets	**61**	56
	8,051	6,837
	21,623	19,830

See accompanying notes to the consolidated financial statements

Consolidated Balance Sheets

As at December 31 (millions of dollars)	2005	2004
Liabilities		
Current liabilities		
Accounts payable and accrued charges (notes 15 and 16)	**958**	949
Market Power Mitigation Agreement rebate payable (note 17)	**–**	439
Revenue limit rebate payable (note 18)	**739**	–
Short-term notes payable (note 7)	**–**	26
Long-term debt due within one year (note 8)	**806**	5
Deferred revenue due within one year	**12**	12
Income and capital taxes payable (note 10)	**81**	12
	2,596	1,443
Long-term debt (note 8)	**3,089**	3,399
Other long-term liabilities		
Fixed asset removal and nuclear waste management (note 9)	**8,759**	8,339
Other post employment benefits and supplementary pension plans (note 11)	**1,212**	1,105
Long-term accounts payable and accrued charges	**183**	212
Deferred revenue	**144**	156
Future income taxes (note 10)	**241**	155
Regulatory liabilities (note 6)	**12**	–
	10,551	9,967
Shareholder's equity		
Common shares	**5,126**	5,126
Retained earnings (deficit)	**261**	(105)
	5,387	5,021
	21,623	19,830

Commitments and Contingencies (notes 2, 5, 7, 8, 9, 10, 12 and 14)

See accompanying notes to the consolidated financial statements

On behalf of the Board of Directors:

Honourable Jake Epp
Chairman

M. George Lewis
Director

Notes to the Consolidated Financial Statements for the Years Ended December 31, 2005 and 2004

1 Description of Business

Ontario Power Generation Inc. was incorporated on December 1, 1998 pursuant to the *Business Corporations Act* (Ontario). As part of the reorganization of Ontario Hydro, under the *Electricity Act, 1998* and the related restructuring of the electricity industry in Ontario, Ontario Power Generation Inc. and its subsidiaries (collectively "OPG" or the "Company") purchased and assumed certain assets, liabilities, employees, rights and obligations of the electricity generation business of Ontario Hydro on April 1, 1999 and commenced operations on that date. Ontario Hydro has continued as Ontario Electricity Financial Corporation ("OEFC"), responsible for managing and retiring Ontario Hydro's outstanding debt and other obligations.

2 Basis of Presentation

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

The consolidated financial statements include the accounts of OPG 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.

Certain of the 2004 comparative amounts have been reclassified from financial statements previously presented to conform to the 2005 financial statement presentation.

3 Summary of Significant Accounting Policies

Cash and Cash Equivalents and Short-Term Investments

Cash and cash equivalents include cash on deposit and money market securities with a maturity of less than 90 days on the date of purchase. All other money market securities with a maturity on the date of purchase that is greater than 90 days, but less than one year, are recorded as short-term investments. These securities are valued at the lower of cost or market.

Interest earned on cash and cash equivalents and short-term investments of $13 million (2004 – $5 million) at an average effective rate of 2.8 per cent (2004 – 2.2 per cent) is offset against interest expense in the consolidated statements of income.

Sales of Accounts Receivable

Asset securitization involves selling assets such as accounts receivable to independent entities or trusts, which buy the receivables and then issue interests in them to investors. These transactions are accounted for as sales, given that control has been surrendered over these assets in return for net cash consideration. For each transfer, the excess of the carrying value of the receivables transferred over the estimated fair value of the proceeds received is reflected as a loss on the date of the transfer, and is included in net interest expense. The carrying value of the interests transferred is allocated to accounts receivable sold or interests retained according to their relative fair values on the day the transfer is made.

Fair value is determined based on the present value of future cash flows. Cash flows are projected using OPG's best estimates of key assumptions, such as discount rates, weighted average life of accounts receivable and credit loss ratios.

As part of the sales of accounts receivable, certain financial assets are retained and consist of interests in the receivables transferred. Any retained interests held in the receivables are accounted for at cost. The receivables are transferred on a fully serviced basis and do not create a servicing asset or liability.

Inventories

Fuel inventory is valued at weighted average cost.

Materials and supplies are valued at the lower of average cost or net realizable value with the exception of critical replacement parts which are unique to nuclear and fossil-fuelled generating stations. The cost of the critical replacement parts inventory is charged to operations on a straight-line basis over the remaining life of the related facilities and is classified in long-term assets.

Fixed Assets and Depreciation

Property, plant and equipment are recorded at cost. Interest costs incurred during construction are capitalized as part of the cost of the asset based on the interest rate on OPG's long-term debt. Expenditures for replacements of major components are capitalized.

Depreciation rates for the various classes of assets are based on their estimated service lives. Any asset removal costs that have not been specifically provided for in current or previous periods are also charged to depreciation expense. Repairs and maintenance are expensed when incurred.

Fixed assets are depreciated on a straight-line basis except for computers, and transport and work equipment, which are depreciated on a declining balance basis as noted below:

Darlington and Pickering B nuclear generating stations	25 years
Pickering A nuclear generating station	42 to 44 years[1]
Fossil generating stations	40 to 50 years[2]
Hydroelectric generating stations	100 years
Administration and service facilities	50 years
Computers, and transport and work equipment assets – declining balance	9% to 40% per year
Major application software	5 years

1. Units 1 and 4 of the Pickering A station are depreciated over a longer operating life as a result of the completion, during the 1980s, of the retubing of the Pickering A station and the refurbishment of Units 1 and 4, completed in 2005 and 2003 respectively.
2. Commencing January 1, 2004, the coal-fired generating stations will be depreciated over the period from 2004 to 2007, due to the expected shutdown of these stations by the end of 2007, with the exception of the Nanticoke generating station which will be depreciated over the period to 2008.

Impairment of Fixed Assets

OPG evaluates its property, plant and equipment for impairment whenever conditions indicate that estimated undiscounted future net cash flows may be less than the net carrying amount of assets. In cases where the undiscounted expected future cash flows are less than the carrying amount, an impairment loss is recognized equal to the amount by which the carrying amount exceeds the fair value. Fair value is determined using expected discounted cash flows when quoted market prices are not available.

Long-Term Portfolio Investments

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

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

Fixed Asset Removal and Nuclear Waste Management Liability

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

On an ongoing basis, the liability is increased by the present value of the variable cost portion of the nuclear waste generated each year, with the corresponding amounts charged to operating expenses. Expenses relating to low and intermediate level waste are charged to depreciation and amortization expense. Expenses relating to the disposal of nuclear used fuel are charged to fuel expense. The liability may also be adjusted due to any changes in the estimated amount or timing of the underlying future cash flows. Upon settlement of the liability, a gain or loss would be recorded.

Accretion arises because liabilities for fixed asset removal and nuclear waste management are reported on a net present value basis. Accretion expense is the increase in the carrying amount of the liabilities due to the passage of time. The resulting expense is included in operating expenses.

The asset retirement cost is capitalized by increasing the carrying value of the related fixed assets. The capitalized cost is depreciated over the remaining useful life of the related fixed assets and is included in depreciation expense.

Nuclear Fixed Asset Removal and Nuclear Waste Management Funds

Pursuant to the Ontario Nuclear Funds Agreement ("ONFA") between OPG and the Province of Ontario, OPG established the Used Fuel Fund and a Decommissioning Fund (together the "Nuclear Funds"). The Used Fuel Fund is intended to fund expenditures associated with the disposal of highly radioactive used nuclear fuel bundles, while the Decommissioning Fund was established to fund expenditures associated with nuclear fixed asset removal and the disposal of low and intermediate level nuclear waste materials. OPG maintains the Nuclear Funds in third party custodial accounts that are segregated from the rest of OPG's assets.

The Nuclear Funds are invested in fixed income and equity securities, which OPG records as long-term investments and accounts for at their amortized cost value. Therefore, gains and losses are recognized only upon the sale of an underlying security. As such, there may be unrealized gains and losses associated with the investments in the Nuclear Funds, which OPG has not recognized in its consolidated financial statements.

Revenue Recognition

All of OPG's electricity generation is sold into the real-time energy spot market administered by the Independent Electricity System Operator ("IESO"). Prior to April 1, 2005, revenue was recorded as electricity was generated and metered based on the spot market sales price, net of the Market Power Mitigation Agreement rebate and hedging activities. At each balance sheet date, OPG computed the average spot energy price that prevailed since the beginning of the current settlement period and recognized a Market Power Mitigation Agreement rebate if the average price exceeded 3.8¢/kilowatt-hour ("kWh"), based on the amount of energy subject to the rebate.

Effective April 1, 2005, the generation from most of OPG's baseload hydroelectric facilities and all of its nuclear facilities became rate regulated. OPG continues to receive the spot market price for the output from its remaining hydroelectric, fossil-fuelled and wind generating stations, subject to a revenue limit. As a result, energy revenue generated from the nuclear facilities is recognized based on a regulated price of 4.95¢/kWh. The regulated price received by OPG for the first 1,900 megawatt hours (MWh) of production from the regulated hydroelectric facilities in any hour is 3.3¢/kWh. Any production from these regulated hydroelectric facilities above 1,900 MWh in any hour receives the Ontario electricity spot market price. The production from OPG's other generating assets remains unregulated and continues to be sold at the Ontario electricity spot market price. However, 85 per cent of the generation output from OPG's other generating assets, excluding the Lennox generating station, Transition – Generation Corporation Designated Rate Options ("TRO") volumes and forward sales as of January 1, 2005, are subject to a revenue limit based on an average price of 4.7¢/kWh. This revenue limit was originally established for a period of 13 months ending April 30, 2006.

OPG also sells into, and purchases from, interconnected markets of other provinces and the U.S. northeast and midwest. All contracts that are not designated as hedges are recorded in the consolidated balance sheets at market value with gains or losses recorded in the consolidated statements of income. Gains and losses on energy trading contracts (including those to be physically settled) are recorded on a net basis in the consolidated statements of income. Accordingly, power purchases of $228 million in 2005 and $170 million in 2004 were netted against revenue.

OPG derives non-energy revenue under the terms of a lease arrangement with Bruce Power L.P. ("Bruce Power") related to the Bruce nuclear generating stations. This includes lease revenues, interest income and revenues for engineering analysis and design, technical and ancillary services. OPG also earns revenue from its joint venture share of the Brighton Beach Power Limited Partnership ("Brighton Beach") related to an energy conversion agreement between Brighton Beach and Coral Energy Canada Inc. ("Coral"). In addition, non-energy revenue includes isotope sales to the medical industry and real estate rentals. Revenues from these activities are recognized as services are provided or products are delivered.

Foreign Currency Translation

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian currency at year-end exchange rates. Any resulting gain or loss is reflected in other revenue.

Derivatives

OPG is exposed to changes in electricity prices associated with a wholesale spot market for electricity in Ontario. To hedge the commodity price risk exposure associated with changes in the wholesale price of electricity, OPG enters into various energy and related sales contracts. These contracts are expected to be effective as hedges of the commodity price exposure on OPG's generation portfolio. Gains or losses on hedging instruments are recognized in income over the term of the contract when the underlying hedged transactions occur. These gains or losses are included in unregulated revenue and are not recorded on the consolidated balance sheets. All contracts not designated as hedges are recorded as assets or liabilities at fair value with changes in fair value recorded in other revenue.

OPG also enters into derivative contracts with major financial institutions to manage the Company's exposure to foreign currency movements. Foreign exchange translation gains and losses on these foreign currency denominated derivative contracts are recognized as an adjustment to the purchase price of the commodity or goods received.

OPG is exposed to changes in market interest rates on debt expected to be issued in the future. OPG uses interest rate derivative contracts to hedge this exposure. Gains and losses on interest rate hedges are recorded as an adjustment to interest expense for the debt being hedged. Gains and losses that do not meet the effectiveness criteria are recorded through net income in the period incurred.

OPG utilizes emission reduction credits ("ERCs") and allowances to manage emissions within the prescribed regulatory limits. ERCs are purchased from trading partners in Canada and the United States. Emission allowances are obtained from the Province and purchased from trading partners in Ontario. The cost of ERCs and allowances are held in inventory and charged to OPG's operations at average cost as part of fuel expense as required. Options to purchase ERCs are accounted for as derivatives and are recorded at estimated market value.

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 derivative instrument 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.

Research and Development

Research and development costs are charged to operations in the year incurred. Research and development costs incurred to discharge long-term obligations such as the nuclear waste management liabilities, for which specific provisions have already been made, are charged to the related liability.

Pension and Other Post Employment Benefits

OPG's post employment benefit programs include a contributory defined benefit registered pension plan, a defined benefit supplementary pension plan, group life insurance, health care and long-term disability benefits. OPG accrues its obligations under pension and other post employment benefit ("OPEB") plans. The obligations for pension and other post retirement benefit costs are determined using the projected benefit method pro-rated on service. The obligation for long-term disability benefits is determined using the projected benefit method on a terminal basis. The obligations are affected by salary levels, inflation, and cost escalation. Pension and OPEB costs and obligations are determined annually by independent actuaries using management's best estimate assumptions. The discount rates used by OPG in determining projected benefit obligations and the costs for the Company's employee benefit plans are based on representative AA corporate bond yields.

Pension fund assets are valued using market-related values for purposes of determining actuarial gains or losses and the expected return on plan assets. The market-related value recognizes gains and losses on equity assets relative to a six per cent assumed real return over a five-year period.

Pension and OPEB costs include current service costs, interest costs on the obligations, the expected return on pension plan assets, adjustments for plan amendments and adjustments for actuarial gains or losses, which result from changes in assumptions and experience gains and losses. Past service costs arising from pension and OPEB plan amendments are amortized on a straight-line basis over the expected average remaining service life of the employees covered by the plan, since OPG will realize the economic benefit over that period. Due to the long-term nature of post-employment liabilities, the excess of the net cumulative unamortized gain or loss, over 10 per cent of the greater of the benefit obligation and the market-related value of the plan assets, is also amortized over the expected average remaining service life.

When the recognition of the transfer of employees and employee-related benefits gives rise to both a curtailment and a settlement, the curtailment is accounted for prior to the settlement. A curtailment is the loss by employees of the right to earn future benefits under the plan. A settlement is the discharge of a plan's liability.

Taxes

Under the *Electricity Act, 1998*, OPG is responsible for making payments in lieu of corporate income and capital taxes to the OEFC. These payments are calculated in accordance with the *Income Tax Act* (Canada) and the *Corporations Tax Act* (Ontario), and are modified by the *Electricity Act, 1998* and related regulations. This effectively results in OPG paying taxes similar to what would be imposed under the federal and Ontario tax acts.

OPG uses the liability method of accounting for income taxes for the unregulated segments of its business. Under the liability method, income taxes are recognized as a result of temporary differences arising from the difference between the tax basis of an asset or liability and its carrying value in the balance sheet, the carry-forward of unused tax losses and income tax reductions. Future income tax assets and liabilities are measured using income tax rates expected to apply in the years in which temporary differences are expected to reverse. The effect on future income tax assets and liabilities of a change in tax rates is included in income in the period the change is substantively enacted. Future income tax assets are evaluated and if realization is not considered 'more likely than not', a valuation allowance is established.

Commencing April 1, 2005, with the introduction of rate regulation, OPG accounts for income taxes related 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 related to the rate regulated segments of its business to the extent that these future income taxes are expected to be recovered in the regulated rates charged to future customers.

OPG makes payments in lieu of property tax on its nuclear and fossil-fuelled generating assets to the OEFC, and also pays property taxes to municipalities.

OPG pays charges on gross revenue derived from the annual generation of electricity from its hydroelectric generating assets. The gross revenue charge ("GRC") includes a fixed percentage charge applied to the annual hydroelectric generation derived from stations located on provincial Crown lands, in addition to graduated rate charges applicable to all hydroelectric stations. GRC costs are included in fuel expense.

Business Segments

As noted in Note 19, OPG changed its definition of business segments on April 1, 2005 from Generation and Energy Marketing to Regulated – Nuclear, Regulated – Hydroelectric and Unregulated Generation. OPG will continue to report other activities, including trading activities, which were previously reported separately, in the Other category. As a result of this change in definition, OPG has reclassified the comparative periods to be consistent with the current presentation of business segments.

Changes in Accounting Policies

Rate Regulated Accounting

In December 2004, the *Electricity Restructuring Act, 2004* (Bill 100) received Royal Assent. A regulation made pursuant to that statute in February 2005 provides that OPG receive regulated prices beginning April 1, 2005, for its baseload hydroelectric and nuclear facilities. This includes electricity generated by 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 generating stations.

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

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

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

Income Taxes

Commencing April 1, 2005, with the introduction of rate regulation, OPG accounts for income taxes related to the rate regulated segments of its business using the taxes payable method.

New Accounting Recommendations

Consolidation of Variable Interest Entities

In September 2004, the CICA amended Accounting Guideline 15, *Consolidation of Variable Interest Entities*, originally issued in June 2003, to harmonize with the revised Financial Accounting Standards Board Interpretation No. 46, *Consolidation of Variable Interest Entities* ("FIN 46R"). The new guideline requires the consolidation of variable interest entities ("VIEs") by the primary beneficiary. A VIE is an entity where (i) its equity investment at risk is insufficient to permit the entity to finance its activities without additional subordinated support from others and/or where certain essential characteristics of a controlling financial interest are not met, and (ii) it does not meet specified exemption criteria. The primary beneficiary is the enterprise that will absorb or receive the majority of the VIEs' expected losses, expected residual returns, or both.

OPG is involved with various joint venture and other arrangements and has sold trade receivables under an asset securitization arrangement. OPG concluded that the joint venture and other arrangements with which it is involved are not VIEs, and that it is not the primary beneficiary of, nor does it have a significant variable interest in, the trust to which it sold trade receivables.

Investment Companies

In January 2004, the CICA issued Accounting Guideline 18, *Investment Companies* ("AcG-18"). The new guideline requires investments owned by entities that meet the investment companies criteria, to be recorded at fair value with gains and losses recognized in net income. During 2005, OPG applied the new guideline to investments that its owns.

Future Accounting Policy Changes

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

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

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

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

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

4 Sale of Accounts Receivable

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

OPG reflected the initial transfer to the trust of the co-ownership interest, and subsequent transfers required by the revolving nature of the securitization, as sales in accordance with CICA Accounting Guideline 12, *Transfer of Receivables*. In accordance with this Guideline, the proceeds of each sale to the trust were deemed to be the cash received from the trust net of the undivided co-ownership interest retained by the Company. For 2005, the Company has recognized pre-tax charges of $9 million (2004 – $8 million) on such sales at an average cost of funds of 3.1 per cent (2004 – 2.6 per cent). As at December 31, 2005, OPG had sold receivables of $300 million from its total portfolio of $668 million.

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

	Principal amount of receivables as at December 31		Average balance of receivables for year ended December 31	
(millions of dollars)	**2005**	2004	**2005**	2004
Total receivables portfolio[1]	**668**	490	**559**	470
Receivables sold	**300**	300	**300**	300
Receivables retained	**368**	190	**259**	170
Average cost of funds			**3.1%**	2.6%

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

An immediate 10 per cent or 20 per cent adverse change in the discount rate would not have a material effect on the current fair value of the retained interest. There were no credit losses for the year ended December 31, 2005 and 2004.

Details of cash flows from securitizations for the years ended December 31 are as follows:

(millions of dollars)	**2005**	2004
Collections reinvested in revolving sales[1]	**3,600**	3,600
Cash flows from retained interest	**3,104**	2,043

1. Given the revolving nature of the securitization, the cash collections received on the receivables securitized are immediately reinvested in additional receivables resulting in no further cash proceeds to the Company over and above the initial cash amount of $300 million. The amounts reflect the cumulative of 12 monthly amounts.

5 Fixed Assets

Depreciation and amortization expense consists of the following:

(millions of dollars)	**2005**	2004
Depreciation and amortization	**748**	758
Nuclear waste management costs	**5**	7
	753	765

Fixed assets consist of the following:

(millions of dollars)	**2005**	2004
Property, plant and equipment		
Nuclear generating stations	**4,754**	4,326
Regulated Hydroelectric generating stations	**4,379**	4,345
Unregulated Hydroelectric generating stations	**3,447**	3,432
Fossil-fuelled generating stations	**1,411**	1,596
Other fixed assets	**833**	850
Construction in progress	**348**	565
	15,172	15,114
Less: accumulated depreciation		
Generating stations	**3,497**	2,935
Other fixed assets	**263**	239
	3,760	3,174
	11,412	11,940

The asset under capital lease was $203 million in 2004 and was included in other fixed assets. There were no assets under capital lease as at December 31, 2005. Accumulated depreciation on the leased asset at December 31, 2004 was $53 million. Interest capitalized at six per cent during the years ended December 31, 2005 and 2004 was $27 million and $30 million, respectively.

Impairment of Long-Lived Assets

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

Pickering A Nuclear Generating Station Units 2 and 3

OPG completed an assessment of the cost, schedule and risks related to the return to service of Units 2 and 3 at the Pickering A nuclear generating station. This included an assessment of the ability of these units to perform at an acceptable capability factor over the remaining 12 to 20 years of operations. This assessment incorporated recent findings from inspection programs with respect to feeder pipe and steam generator degradation mechanisms, and potential degradation of the calandria vault components, all of which could impact the future capability factor, operating costs and the life of the units. Upon consideration of the scope of the refurbishment work, the costs and the risks related to the return to service of these two units, and the Company's focus on improving the performance of its other nuclear units, OPG's Board of Directors decided that while technically feasible, the return to service of these units was not justified on a commercial basis. Accordingly, OPG recorded an impairment loss of $63 million in the second quarter of 2005 related to the carrying amount of these two units including construction in progress. In addition to the impairment loss for these two units, OPG recorded OM&A expenses of $57 million related to the write-off of inventory identified as excess or unusable, as a result of not returning Units 2 and 3 to service.

OPG expects to recover the amounts recorded in the deferral account relating to non-capital costs incurred after January 1, 2005 associated with the return to service of Units 2 and 3. As at December 31, 2005, the deferral account relating to Units 2 and 3 was $19 million.

As a result of the decision not to proceed with the return to service of these two units, OPG continues to assess the need to provide for any additional costs, including the cost associated with preparing the units for safe storage, any impacts on cost estimates for asset retirement obligation and any other additional exit costs. Such charges may have a significant impact on operating results in future periods.

Lennox Generating Station

As a result of the Government's "Request for Information/Request for Proposal for 2,500 MW of New Clean Generation and Demand Side Management Projects" released in September 2004 and the related contractual arrangements, future wholesale electricity market revenue is expected to be lower than previously anticipated. As a relatively high variable cost plant, the Lennox generating station will not be able to recover its fixed operating costs and its carrying value from the wholesale electricity market in the future. Given these factors, OPG had initiated discussions with the Province, with the expectation of entering into a contractual arrangement for the recovery of the annual fixed operating costs and the carrying value of the Lennox generating station. In March 2005, OPG was advised by the Province that it would continue to support OPG in negotiating an arrangement that would allow for the recovery of fixed operating costs, but that the Province would not support an arrangement that would allow for the recovery of the carrying value of the Lennox generating station. As a result of this change in circumstance, OPG recorded the impairment loss of $202 million in the first quarter of 2005. OPG has since negotiated a contract with the Independent Electricity System Operator ("IESO"), pursuant to the market rules, to recover its operating costs for a one-year period ending September 30, 2006. The contract with the IESO has been submitted to the OEB for approval.

6 Regulatory Assets and Liabilities

OPG recorded the following regulatory assets and liabilities as at December 31, 2005:

(millions of dollars)	2005
Regulatory assets	
Pickering A return to service costs deferral account	261
Ancillary services revenue variance account	5
Total regulatory assets	266
Regulatory liabilities	
Hydroelectric production variance account	4
Other	8
Total regulatory liabilities	12

Pickering A Return to Service Costs

Effective January 1, 2005, in accordance with regulations pursuant to the *Electricity Restructuring Act, 2004*, OPG is required to establish a deferral account in connection with non-capital costs that are associated with the return to service of units at the Pickering A nuclear generating station. As a result, the change in accounting was prospectively adopted on January 1, 2005, with no retroactive adoption. As at December 31, 2005, the deferral account was $261 million, consisting of non-capital costs, net of amortization, of $228 million relating to Unit 1, $19 million relating to Units 2 and 3, $11 million of general return to service costs, and interest of $7 million accreted at the average cost of debt of six per cent. Upon OPG becoming subject to regulated prices established by the OEB, expected after March 31, 2008, the OEB is directed by the regulation to ensure that OPG recovers any balance in the deferral account on a straight-line basis over a period not to exceed 15 years.

In November 2005, as a result of the return to commercial service of Unit 1 at the Pickering A nuclear generating station, OPG commenced amortization of the Pickering A return to service regulatory asset to OM&A expenses. The basis for amortization is consistent with that reflected in interim regulated rates and resulted in OPG recording $4 million in OM&A expenses as at December 31, 2005.

Had OPG not charged costs to the deferral account as required by the regulations, an additional $254 million would have been charged to OM&A expense and $7 million to net interest expense during 2005.

Variance Accounts

Effective April 1, 2005, in accordance with the regulations pursuant to the *Electricity Restructuring Act, 2004,* OPG was directed to establish variance accounts for costs incurred on or after April 1, 2005 that are associated with differences in hydroelectric electricity production due to differences between forecast and actual water conditions, changes in nuclear electricity production due to unforeseen changes to the law or to unforeseen technological changes, changes to revenues assumed for ancillary revenues from the regulated facilities, acts of God (including severe weather events), and transmission outages and transmission restrictions. OPG recorded an asset as at December 31, 2005 of $5 million, reflecting ancillary services revenue that was unfavourable compared to that forecasted for 2005. OPG recorded a liability as at December 31, 2005 of $4 million, reflecting water conditions that were favourable compared to those forecasted for 2005. Upon OPG becoming subject to regulated prices established by the OEB, the OEB is directed by the regulation to ensure recovery to the extent that the OEB is satisfied that the costs recorded in the account were prudently incurred and accurately recorded. Any balances approved by the OEB will be amortized over a period not to exceed three years.

Had OPG not accounted for the variances as a regulatory asset and liability, revenue for 2005 would have been lower by $1 million.

The other regulatory liability consists of a portion of non-regulated revenue earned by OPG's regulated assets, which will result in a reduction of future regulated rates to be established by the OEB.

7 Short-Term Credit Facilities

OPG's current 364-day term $1 billion revolving committed bank credit facility was renewed on May 24, 2005. The new facility is divided into two tranches – a $500 million 364-day term tranche maturing May 23, 2006, and a $500 million three-year term tranche maturing May 23, 2008. The total credit facility will continue to be used primarily as support for notes issued under OPG's commercial paper program. As at December 31, 2005, OPG had no borrowings outstanding under this commercial paper program (2004 – $26 million). As at December 31, 2005 and 2004, OPG had no other outstanding borrowing under this facility.

OPG also maintains $26 million (2004 – $26 million) in short-term uncommitted overdraft facilities as well as $215 million (2004 – $200 million) of short-term uncommitted credit facilities, which support the issuance of Letters of Credit. OPG uses Letters of Credit to support supplementary pension plans and is required to post the Letters of Credit as collateral with Local Distribution Companies ("LDCs") as prescribed by the OEB's Retail Settlement Code. At December 31, 2005, there were approximately $157 million (2004 – $155 million) of Letters of Credit issued for the supplementary pension plans and collateral requirements to the LDCs.

8 Long-Term Debt

Long-term debt consists of the following:

(millions of dollars)	**2005**	2004
Notes payable to the OEFC	**3,695**	3,200
Capital lease obligations	**–**	3
Share of non-recourse limited partnership debt	**200**	201
	3,895	3,404
Less: due within one year		
Notes payable to the OEFC	**800**	–
Capital lease obligations	**–**	3
Share of limited partnership debt	**6**	2
	806	5
Long-term debt	**3,089**	3,399

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

The maturity dates as at December 31, 2005 for notes payable to the OEFC are as follows:

		Principal Outstanding (millions of dollars)		
Year of Maturity	Interest Rate (%)	Senior Notes	Subordinated Notes	Total
2006	5.70%	800	–	800
2007	5.85%	400	–	400
2008	5.90%	400	–	400
2009	6.01%	350	–	350
2010	6.00%	595	375	970
2011	6.65%	–	375	375
2012	5.72%	400	–	400
		2,945	750	3,695

In December 2004, OPG reached an agreement with the OEFC to defer payment on the $500 million principal amount of senior notes maturing in March and September 2005 by extending the maturity dates by five years. The interest rates remain unchanged. In March 2005, the Company reached an agreement with the OEFC to obtain additional financing up to $600 million, which can be drawn until March 31, 2006. In April 2005, $400 million was drawn under this facility, with a seven-year term.

The Company also reached an agreement with the OEFC to satisfy, through the issue of additional senior notes of $95 million and $98 million respectively, to mature in 2010, its $95 million interest obligation due in March 2005 and the $98 million interest obligation due in September 2005 related to the debt owing to the OEFC of $3.2 billion. As a result of an improved liquidity position, OPG elected to pay the interest due in September 2005 and not issue the $98 million note.

Interest paid in 2005 was $235 million (2004 – $218 million), of which $220 million relates to interest paid on long-term debt (2004 – $213 million).

In September 2005, OPG reached an agreement with the OEFC to provide debt financing for the Niagara tunnel project. The funding, which is up to $1 billion over the duration of the project, will be in the form of 10-year notes, which will be issued quarterly to meet the project's obligations. Interest will be fixed for each note issued at the time of advance at a rate equal to the prevailing Benchmark Government of Canada 10-Year Bond, plus a credit spread determined by the OEFC based on a survey of market rates.

In October 2005, OPG reached a similar agreement with the OEFC to finance the Thunder Bay Gas Conversion project. There will be up to $95 million available to OPG under this credit facility, that will be drawn as needed over the projected two-year construction period. OPG is expected to make its first draw under this facility in the first quarter of 2006.

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:

(millions of dollars)	**2005**	2004
Liability for nuclear used fuel management	**4,940**	4,693
Liability for nuclear decommissioning and low and intermediate level waste management	**3,627**	3,457
Liability for non-nuclear fixed asset removal	**192**	189
Fixed asset removal and nuclear waste management liability	**8,759**	8,339

The change in the fixed asset removal and nuclear waste management liability for the years ended December 31, 2005 and 2004, is as follows:

(millions of dollars)	**2005**	2004
Liability, beginning of year	**8,339**	7,921
Increase in liability due to accretion	**476**	453
Increase in liability due to nuclear used fuel and nuclear waste management variable expenses	**34**	35
Fixed asset removal of partnership interests	**–**	1
Liabilities settled by expenditures on waste management	**(90)**	(71)
Liability, end of year	**8,759**	8,339

OPG's asset retirement obligations are comprised of expected costs to be incurred up to and upon termination of operations and the closure of nuclear and fossil-fuelled generating plant facilities. Costs will be incurred for activities such as dismantling, demolition and disposal of facilities and equipment, remediation and restoration of sites and the ongoing and long-term management of nuclear used fuel and low and intermediate level waste material.

The following costs are recognized as a liability:

- The present value of the costs of dismantling the nuclear and fossil-fuelled production facilities at the end of their useful lives
- The present value of the fixed cost portion of any nuclear waste management programs that are required based on the total volume of waste expected to be generated over the assumed life of the stations
- The present value of the variable cost portion of any nuclear waste management program to take into account actual waste volumes incurred to date.

The determination of the accrual for fixed asset removal and nuclear waste management costs requires significant assumptions, since these programs run for many years. Plant closures are projected to occur between one and 14 years from today, depending on the plant. Current plans include cash flow estimates to 2057 for decommissioning nuclear stations and to approximately 2100 for nuclear used fuel management. The undiscounted amount of estimated cash flows associated with the liability expected to be incurred up to and upon closure of generating stations is approximately $20 billion. The discount rate used to calculate the present value of the liabilities at December 31, 2005 was 5.75 per cent (2004 – 5.75 per cent) and the cost escalation rates ranged from two per cent to four per cent. Under the terms of the lease agreement with Bruce Power, OPG continues to be responsible for the nuclear fixed asset removal and nuclear waste management liabilities associated with the Bruce nuclear generating stations.

The significant assumptions underlying operational and technical factors used in the calculation of the accrued liabilities are subject to periodic review. The estimate of the liability is being updated in 2006. Changes to these assumptions, including changes to assumptions on the timing of the programs, financial indicators or the technology employed, could result in significant changes to the value of the accrued liabilities. With programs of this duration and the evolving technology to handle the nuclear waste, there is a significant degree of uncertainty surrounding the measurement accuracy of the costs for these programs, which may increase or decrease over time.

Liability for Nuclear Used Fuel Management Costs

The liability for nuclear used fuel management represents the cost of managing the highly radioactive used nuclear fuel bundles. The current assumptions that have been used to establish the accrued used fuel costs include long-term management of the spent fuel bundles through deep geological disposal; an in-service date of 2035 for used nuclear fuel disposal facilities; and an average transportation distance of 1,000 kilometres between nuclear generating facilities and the disposal facilities. Alternatives to deep geological disposal have been studied by Canadian nuclear utilities via the Nuclear Waste Management Organization as part of the options study required by the federal Nuclear Fuel Waste Act (Canada) ("NFWA"). The options study was submitted to the federal government in November 2005. The federal government will decide which management alternative should be followed. The pending decision could have a significant impact on OPG's estimate of the liability.

Liability for Nuclear Decommissioning and Low and Intermediate Level Waste Management Costs

The liability for nuclear decommissioning and low and intermediate level waste management represents the estimated costs of decommissioning nuclear generating stations after the end of their service lives, as well as the cost of managing low and intermediate level radioactive wastes generated by the nuclear stations. The significant assumptions used in estimating future nuclear fixed asset removal costs include decommissioning of nuclear generating stations on a deferred dismantlement basis where the reactors will remain in a safe storage state for a 30-year period prior to a 10-year dismantlement period. Current plans assume that low and intermediate level waste arising during decommissioning will be disposed of at the facilities developed for disposal of operational low and intermediate level waste.

The life cycle costs of low and intermediate level waste management include the costs of processing and storage of such radioactive wastes during and following the operation of the nuclear stations, as well as the costs of ultimate long-term disposal of these wastes. The current assumptions used to establish the accrued low and intermediate level waste management costs include: an in-service date of 2015 for disposal facilities for low level waste; co-locating short-lived intermediate level waste with low level waste starting in 2015; and co-locating long-lived intermediate level waste with used fuel starting in 2035. Plans are currently proceeding for development of a deep geologic repository at the Western Waste Management Facility. Agreements are in place with the Municipality of Kincardine for this repository.

Liability for Non-Nuclear Fixed Asset Removal Costs
The liability for non-nuclear fixed asset removal is based on third-party cost estimates after an in-depth review of active plant sites and an assessment of required clean-up and restoration activities. This liability represents the estimated costs of decommissioning fossil-fuelled generating stations at the end of their service lives. The estimated retirement date of these stations is between 2007 and 2034.

In addition to the $95 million liability for active sites, OPG also has an asset retirement obligation liability of $97 million for decommissioning and restoration costs associated with plant sites that have been divested or are no longer in use.

OPG has no legal obligation associated with the decommissioning of its hydroelectric generating facilities. Also, the costs cannot be reasonably estimated because of the long service life of these assets. With either maintenance efforts or rebuilding, the water control structures are assumed to be used for the foreseeable future. Accordingly, OPG has not recognized a liability for the decommissioning of its hydroelectric generating facilities.

Ontario Nuclear Funds Agreement
OPG sets aside funds to be used specifically for discharging its nuclear fixed asset removal and nuclear waste management liabilities. In July 2003, OPG and the Province completed arrangements, pursuant to the ONFA. To comply with the ONFA, OPG established the Nuclear Funds. OPG jointly oversees the investment management of the Nuclear Funds with the Province. The assets of the Nuclear Funds are maintained in third party custodian accounts that are segregated from the rest of OPG's assets.

The Decommissioning Fund will be used 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. The initial funding of the Decommissioning Fund was intended to be sufficient to fully discharge the 1999 estimate of the liability. OPG bears the risk and liability for cost estimate increases and fund earnings in the Decommissioning Fund.

The Used Fuel Fund will be used to fund future costs of long-term nuclear used fuel waste management. OPG is responsible for the risk and liability for cost increases for used fuel waste management, subject to graduated liability thresholds specified in the ONFA, which limit OPG's total financial exposure at approximately $6 billion, a present value amount at April 1, 1999 (approximately $8.8 billion in 2005 dollars) based on used fuel bundle projections of 2.23 million bundles consistent with the station lives included within the initial financial reference plan. OPG makes quarterly payments to the Used Fuel Fund over the life of its nuclear generating stations, as specified in the ONFA. Required funding for 2005 under the ONFA was $454 million, including a contribution to The Ontario NFWA Trust (the "Trust"). In 2005, an amount of $150 million was directed to the Trust to meet the 2005 requirement of $100 million and $50 million was directed towards the 2006 requirement.

The NFWA was proclaimed into force in November 2002. In accordance with the NFWA, the Nuclear Waste Management Organization was formed to prepare and review alternatives, and to provide recommendations to the federal government for long-term management of nuclear fuel waste by November 2005. The federal government will select the option for dealing with the long-term management of nuclear fuel waste based on submitted plans. As required under the NFWA, OPG made an initial deposit of $500 million into the Trust in November 2002. The NFWA also requires OPG to make annual contributions of $100 million to the Trust, to be deposited into the Trust no later than the November anniversary of the NFWA. To comply with this requirement, OPG contributed $100 million to the Trust in each of 2003 and 2004 and $150 million in 2005 ($50 million funded on December 31, 2005 as part of OPG's $100 million funding requirement for the November 2005 to November 2006 period). Under the NFWA, OPG must continue to deposit $100 million annually into the Trust until the federal government has approved a long-term plan. Future contributions to the Trust beyond 2005 will be dependent on the direction chosen by the federal government based on the recommendations submitted in November 2005. Given that the Trust forms part of the Used Fuel Fund, contributions to the Trust, as required by the NFWA, are applied towards the ONFA payment obligations.

As required by the *Nuclear Safety and Control Act* (Canada), and under the terms of the ONFA, the Province issued a guarantee to the Canadian Nuclear Safety Commission ("CNSC"), on behalf of OPG, for up to $1,510 million. This is a guarantee that there will be sufficient funds available to discharge the current nuclear decommissioning and waste management liabilities. The provincial guarantee will supplement the Used Fuel Fund and the Decommissioning Fund until they have accumulated sufficient funds to cover the accumulated liabilities for nuclear decommissioning and waste management. The guarantee, taken together with the Used Fuel Fund and Decommissioning Fund, was in satisfaction of OPG's nuclear licensing requirements with the CNSC. OPG pays the Province an annual guarantee fee of 0.5 per cent of the amount guaranteed by the Province. OPG paid the annual guarantee fee for 2005 of $8 million in the first quarter of 2005.

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"). The difference between the committed return on the Used Fuel Fund and the actual market return, based on the fair value of fund assets, which includes realized and unrealized returns, is due to or due from the Province. Since OPG accounts for the investments in the segregated funds on an amortized cost basis, the amount due to or due from the Province recorded in the consolidated financial statements is the difference between the committed return and the actual return based on realized returns only. At December 31, 2005, the Used Fuel Fund accounts included an amount due to the Province of $4 million (2004 – $4 million). If the investments in the Used Fuel Fund were accounted for at fair market value in the consolidated financial statements, at December 31, 2005, there would be an amount due to the Province of $306 million (2004 – $156 million).

Under the ONFA, a rate of return target of 5.75 per cent per annum was established for the Decommissioning Fund, subject to changes in the ONFA Reference Plan. If the rate of return deviates from 5.75 per cent, or if the estimate of the liabilities changes under the current approved ONFA Reference Plan, the Decommissioning Fund may become over or underfunded. Under the ONFA, if there is a surplus in the Decommissioning Fund such that the liabilities, as defined by the Current Approved ONFA Reference Plan, are at least 120 per cent funded, OPG may direct up to 50 per cent of the surplus over 120 per cent as a contribution to the Used Fuel Fund, and the OEFC is entitled to a distribution of an equal amount. In addition, upon termination of the ONFA, the Province has a right to any excess funds, which is the extent to which the fair market value of the Decommissioning Fund exceeds the estimated completion costs approved under the Current Approved ONFA Reference Plan. At December 31, 2005, the balance of the Decommissioning Fund, on an amortized cost basis, exceeded the estimated completion costs under the Current Approved ONFA Reference Plan. The Decommissioning Fund had an excess of $7 million due to the Province on an amortized cost basis. If the investments in the Decommissioning Fund were accounted for at fair market value in the consolidated financial statements at December 31, 2005, and the Decommissioning Fund was terminated under the ONFA, there would be an amount due to the Province of $484 million (2004 – $249 million).

The nuclear fixed asset removal and nuclear waste management funds as at December 31, 2005 and 2004, consist of the following:

	Amortized Cost Basis		Fair Value	
(millions of dollars)	**2005**	2004	**2005**	2004
Decommissioning Fund	**4,106**	3,858	**4,583**	4,131
Due to Province – Decommissioning Fund	**(7)**	–	**(484)**	(249)
	4,099	3,858	**4,099**	3,882
Used Fuel Fund[1]	**2,693**	2,122	**2,995**	2,274
Due (to) from Province – Used Fuel Fund	**(4)**	(4)	**(306)**	(156)
	2,689	2,118	**2,689**	2,118
	6,788	5,976	**6,788**	6,000

1. The Ontario NFWA Trust represents $1,003 million as at December 31, 2005 (2004 – $794 million) of the Used Fuel Fund on an amortized cost basis.

The amortized cost and fair value of the securities invested in the segregated funds, which include the Used Fuel Fund and Decommissioning Fund, as at December 31, 2005 and 2004 are as follows:

	Amortized Cost Basis		Fair Value	
(millions of dollars)	**2005**	2004	**2005**	2004
Cash and cash equivalents and short-term investments	**516**	211	**515**	211
Marketable equity securities	**3,772**	3,056	**4,547**	3,472
Bonds and debentures	**1,757**	723	**1,762**	732
Receivable from the OEFC	**759**	1,993	**759**	1,993
Administrative expense payable	**(5)**	(3)	**(5)**	(3)
	6,799	5,980	**7,578**	6,405
Due to Province – Decommissioning Fund	**(7)**	–	**(484)**	(249)
Due to Province – Used Fuel Fund	**(4)**	(4)	**(306)**	(156)
Total	**6,788**	5,976	**6,788**	6,000

The bonds and debentures held in the Used Fuel Fund and the Decommissioning Fund as at December 31, 2005 and 2004 mature according to the following schedule:

	Fair Value	
(millions of dollars)	**2005**	2004
Less than 1 year	**–**	–
1 – 5 years	**769**	259
5 – 10 years	**485**	233
More than 10 years	**508**	240
Total maturities of debt securities	**1,762**	732
Average yield	**4.3%**	4.1%

The receivable of $759 million (2004 - $1,993 million) from the OEFC does not have a specified maturity date. The effective rate of interest on the OEFC receivable was 5.8 per cent in 2005 (2004 – 5.3 per cent).

10 Income taxes

Commencing April 1, 2005, OPG accounts for income taxes related 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 related to the rate regulated segments of its business to the extent that the future income taxes are expected to be recovered in the regulated rates charged to future customers. As part of the transition, on April 1, 2005, OPG reversed the net future income tax asset balance of $74 million relating to the rate regulated segments of its business, and recognized the amount as an extraordinary loss in determining net income. The extraordinary item reduced basic and diluted earnings per share for the year ended December 31, 2005 by $0.29 per share.

A reconciliation between the statutory and the effective rate of income taxes is as follows:

(millions of dollars)	**2005**	2004
Income (loss) before income taxes	**558**	(38)
Combined Canadian federal and provincial statutory income tax rates, including surtax	**36.1%**	36.1%
Statutory income tax rates applied to accounting income	**202**	(14)
Increase (decrease) in income taxes resulting from:		
Large corporations tax in excess of surtax	**28**	30
Lower future tax rate on temporary differences	**(12)**	(3)
Non-taxable income items	**7**	(4)
Unrecorded future income tax related to regulated operations	**(157)**	–
Change in income tax positions	**50**	–
Change in future income tax asset valuation allowance	**–**	(93)
Other	**–**	4
	(84)	(66)
Income tax expense (recovery)	**118**	(80)
Effective rate of income taxes	**21.1%**	210.5%

Prior to 2004, OPG had established a valuation allowance of $93 million to recognize that it was more likely than not that this amount of future income taxes recoverable would not be realized in light of consecutive taxable losses in preceding years. In 2004, the valuation allowance was reduced by $93 million to nil as a consequence of the introduction of rate regulation. With the intended elimination of the future income tax assets and liabilities of the regulated business upon inception of rate regulation on April 1, 2005, it was expected that there would be a significant future income tax liability position remaining in the unregulated business. This expected future income tax liability position enabled OPG to recognize, in 2004, the $93 million in future income tax assets. This resulted in a reduction in the 2004 income tax provision which did not occur in 2005.

OPG has taken certain filing positions for corporate income and capital taxes that may be challenged on audit and possibly disallowed and result in a significant increase in the tax obligation upon reassessment. During 2005, OPG recorded an income tax charge of $50 million to provide for a change in income tax liabilities related to certain income tax positions that the Company has taken in prior years. There is still uncertainty around the amount of the tax provision, and Management is not able to determine the impact of that uncertainty on the consolidated financial statements.

Significant components of the provision for income tax expense (recovery) are presented in the table below:

(millions of dollars)	**2005**	2004
Current income tax expense	**80**	21
Future income tax expense (benefits):		
Change in temporary differences	**(51)**	50
Non-capital loss carry-forward	**88**	(67)
Valuation allowance (reversal)	**–**	(93)
Other	**1**	9
	38	(101)
Income tax expense (recovery)	**118**	(80)

The income tax effects of temporary differences that give rise to future income tax assets and liabilities are presented in the table below:

(millions of dollars)	**2005**	2004
Future income tax assets:		
Fixed asset removal and nuclear waste management liabilities	**27**	2,806
Other liabilities and assets	**107**	446
Non-capital loss carry-forward	**98**	168
Future recoverable Ontario minimum tax	**37**	42
	269	3,462
Future income tax liabilities:		
Fixed assets	**351**	1,211
Fixed asset removal and nuclear waste management fund	**–**	2,039
Other liabilities and assets	**141**	323
	492	3,573
Net future income tax liabilities	**223**	111
Represented by:		
Current portion (asset)	**(18)**	(44)
Long-term portion	**241**	155
	223	111

The following table summarizes the consolidated statement of income and balance sheet amounts under the method used by the Company to account for income taxes compared to what would have been reported had OPG applied the liability method for the regulated business for 2005:

(millions of dollars)	As Stated	Liability Method
Future income tax expense	**38**	195
Extraordinary item	**74**	–
Current portion (assets)	**(18)**	(38)
Long-term portion	**241**	344

Had OPG continued to use the liability method of accounting for income taxes for the regulated business, the future tax expense for the year ended December 31, 2005 would have increased by $157 million with a corresponding increase in the future income tax liability.

At December 31, 2005, OPG had available approximately $280 million (2004 – $549 million) of non-capital loss carry-forwards. The non-capital loss carry-forward is related to the following taxation years:

(millions of dollars)	Loss-Carry Forward	Expiry Date
2003	33	2010
2004	247	2014

The amount of cash income taxes paid during 2005 was $20 million (2004 – $17 million).

11 Benefit Plans

The post employment benefit programs include pension, group life insurance, health care and long-term disability benefits. The registered pension plan is a contributory defined benefit plan covering most employees and retirees. Pension fund assets include equity securities and corporate and government debt securities, real estate and other investments which are managed by professional investment managers. The fund does not invest in equity or debt securities issued by OPG. The supplementary pension plans are defined benefit plans covering certain employees and retirees.

Pension and OPEB obligations are impacted by factors including interest rates, adjustments arising from plan amendments, changes in assumptions and experience gains or losses. The pension and OPEB obligations, and the pension fund assets, are measured at December 31, 2005.

	Registered and Supplementary Pension Plans		Other Post Employment Benefits	
	2005	2004	**2005**	2004
Weighted Average Assumptions – Benefit Obligation at Year End				
Rate used to discount future benefits	**5.00%**	6.00%	**4.97%**	5.88%
Salary schedule escalation rate	**3.00%**	3.25%	**–**	–
Rate of cost of living increase to pensions	**2.00%**	2.25%	**–**	–
Initial health care trend rate	**–**	–	**7.76%**	7.03%
Ultimate health care trend rate	**–**	–	**4.68%**	4.46%
Year ultimate rate reached	**–**	–	**2014**	2014
Rate of increase in disability benefits	**–**	–	**2.00%**	2.25%

	Registered and Supplementary Pension Plans		Other Post Employment Benefits	
	2005	2004	**2005**	2004
Weighted Average Assumptions – Cost for the Year				
Expected return on plan assets net of expenses	**7.00%**	7.00%	**–**	–
Rate used to discount future benefits	**6.00%**	6.25%	**5.88%**	6.17%
Salary schedule escalation rate	**3.25%**	3.25%	**–**	–
Rate of cost of living increase to pensions	**2.25%**	2.25%	**–**	–
Initial health care trend rate	**–**	–	**7.03%**	6.33%
Ultimate health care trend rate	**–**	–	**4.46%**	4.46%
Year ultimate rate reached	**–**	–	**2014**	2010
Rate of increase in disability benefits	**–**	–	**2.25%**	2.25%
Average remaining service life for employees (years)	**11**	12	**11**	12

	Registered Pension Plan		Supplementary Pension Plans		Other Post Employment Benefits	
(millions of dollars)	**2005**	2004	**2005**	2004	**2005**	2004
Changes in Plan Assets						
Fair value of plan assets at beginning of year	**7,056**	6,449	**–**	–	**–**	–
Contributions by employer	**254**	154	**7**	6	**58**	54
Contributions by employees	**56**	52	**–**	–	**–**	–
Actual return on plan assets net of expenses	**858**	693	**–**	–	**–**	–
Settlements	**(2)**	(4)	**–**	–	**–**	–
Benefit payments	**(301)**	(288)	**(7)**	(6)	**(58)**	(54)
Fair value of plan assets at end of year	**7,921**	7,056	**–**	–	**–**	–
Changes in Projected Benefit Obligation						
Projected benefit obligation at beginning of year	**7,663**	7,046	**144**	117	**1,499**	1,307
Employer current service costs	**163**	143	**7**	8	**47**	41
Contributions by employees	**56**	52	**–**	–	**–**	–
Interest on projected benefit obligation	**461**	442	**9**	7	**88**	82
Past service costs	**–**	–	**–**	–	**1**	–
Curtailment loss (gain)	**–**	2	**–**	–	**–**	(1)
Settlement gain	**(2)**	(4)	**–**	–	**–**	–
Benefit payments	**(301)**	(288)	**(7)**	(6)	**(58)**	(54)
Net actuarial loss (gain)	**1,055**	270	**(9)**	18	**488**	124
Projected benefit obligation at end of year	**9,095**	7,663	**144**	144	**2,065**	1,499
Funded Status – Deficit at end of year	**(1,174)**	(607)	**(144)**	(144)	**(2,065)**	(1,499)

	2005	2004
Registered pension plan fund asset investment categories		
Equities	**64%**	65%
Fixed income	**33%**	33%
Cash and short-term	**3%**	2%
Total	**100%**	100%

The assets of the OPG pension fund are allocated among three principal investment categories. Furthermore, equity investments are diversified across Canadian, U.S. and non-North American stocks. The fund also has a small real estate portfolio that is less than one per cent of plan assets.

Based on the most recently filed actuarial valuation, as at January 1, 2005, there was an unfunded liability on a going-concern basis of $465 million and a deficiency on a wind-up basis of $1,979 million. In the previously filed actuarial valuation, as at April 1, 2002, there was a surplus of $262 million on a going-concern basis and $204 million on a wind-up basis.

The supplementary plans are not funded, but are secured by letters of credit totalling $138 million (2004 – $125 million).

	Registered Pension Plan		Supplementary Pension Plans		Other Post Employment Benefits	
(millions of dollars)	**2005**	2004	**2005**	2004	**2005**	2004
Reconciliation of Funded Status to Accrued Benefit Asset (Liability)						
Funded status – deficit at end of year	**(1,174)**	(607)	**(144)**	(144)	**(2,065)**	(1,499)
Unamortized net actuarial loss	**1,737**	1,012	**18**	28	**885**	422
Unamortized past service costs	**100**	119	**4**	5	**16**	18
Accrued benefit asset (liability) at end of year	**663**	524	**(122)**	(111)	**(1,164)**	(1,059)
Short-term portion	**–**	–	**(7)**	(6)	**(67)**	(59)
Long-term portion	**663**	524	**(115)**	(105)	**(1,097)**	(1,000)

	Registered Pension Plan		Supplementary Pension Plans		Other Post Employment Benefits	
(millions of dollars)	**2005**	2004	**2005**	2004	**2005**	2004
Components of Cost Recognized						
Current service costs	**163**	143	**7**	8	**47**	41
Interest on projected benefit obligation	**461**	442	**9**	7	**88**	82
Expected return on plan assets net of expenses	**(527)**	(511)	**–**	–	**–**	–
Curtailment loss (gain)	**–**	2	**–**	–	**–**	(1)
Amortization of past service costs	**18**	18	**1**	1	**3**	3
Amortization of net actuarial loss	**–**	–	**1**	–	**25**	15
Cost recognized	**115**	94	**18**	16	**163**	140

	Registered Pension Plan		Supplementary Pension Plans		Other Post Employment Benefits	
(millions of dollars)	**2005**	2004	**2005**	2004	**2005**	2004
Components of Cost Incurred and Recognized						
Current service costs	**163**	143	**7**	8	**47**	41
Interest on projected benefit obligation	**461**	442	**9**	7	**88**	82
Actual return on plan assets net of expenses	**(858)**	(693)	**–**	–	**–**	–
Curtailment loss (gain)	**–**	2	**–**	–	**–**	(1)
Past service costs	**–**	–	**–**	–	**1**	–
Net actuarial loss (gain)	**1,055**	270	**(9)**	18	**488**	124
Cost incurred in year	**821**	164	**7**	33	**624**	246
Differences between costs incurred and recognized in respect of:						
Actual return on plan assets net of expenses	**331**	182	**–**	–	**–**	–
Past service costs	**18**	18	**1**	1	**2**	3
Net actuarial (gain) loss	**(1,055)**	(270)	**10**	(18)	**(463)**	(109)
Cost recognized	**115**	94	**18**	16	**163**	140

A one per cent increase or decrease in the health care trend rate would result in an increase in the service and interest components of the 2005 OPEB cost recognized of $26 million (2004 – $21 million) or a decrease in the service and interest components of the 2005 OPEB cost recognized of $20 million (2004 – $19 million), respectively. A one per cent increase or decrease in the health care trend rate would result in an increase in the projected OPEB obligation at December 31, 2005 of $343 million (2004 – $221 million) or a decrease in the projected OPEB obligation at December 31, 2005 of $266 million (2004 – $175 million).

12 Financial Instruments

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

Trading activities and liquidity in the Ontario electricity market have been limited as companies are generally entering only into short-term contracts. As a result, forward pricing information for contracts may not accurately represent the cost to enter into these contracts. For Ontario-based contracts that are not entered into for hedging purposes, OPG established liquidity reserves against the fair market value of the assets and liabilities equal to the gain or loss on these contracts. These reserves increased trading revenue by $4 million during 2005 (2004 – decreased by $2 million). Contracts for transactions outside of Ontario continue to be carried on the consolidated balance sheets as assets or liabilities at fair value, with changes in fair value recorded in trading revenue as gains or losses.

Derivative Instruments Used for Hedging Purposes

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

(millions of dollars except where noted)	**Notional Quantity 2005**	**Terms 2005**	**Fair Value 2005**	Notional Quantity 2004	Terms 2004	Fair Value 2004
(Loss)						
Electricity derivative instruments	**4.1 TWh**	**1–2 yrs**	**(125)**	10.4 TWh	1–3 yrs	(71)
Foreign exchange derivative instruments	**U.S. $15**	**Jan/06**	**–**	U.S. $10	Jan/05	–
Interest rate hedges	**400**	**1–15 yrs**	**(7)**	–	–	–

OPG entered into a number of forward start interest rate swap agreements to hedge against the effect of future interest rate movement based on the anticipated future borrowing requirement for the Niagara tunnel project. These transactions are ordinarily accounted for as hedges, however, approximately $5 million was charged to current period operations for those hedges that did not meet the effectiveness criteria during 2005. The remaining loss was deferred.

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 December 31, 2005 was U.S. $0.87 (2004 – U.S. $0.81) for every Canadian dollar.

Derivative Instruments Not Used for Hedging Purposes

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

(millions of dollars except where noted)	**Notional Quantity 2005**	**Fair Value 2005**	Notional Quantity 2004	Fair Value 2004
Foreign exchange derivative	**U.S. $3**	**–**	–	–
Commodity derivative instruments				
Assets	**3.3 TWh**	**13**	7.9 TWh	12
Liabilities	**1.1 TWh**	**(37)**	1.3 TWh	(12)
		(24)		–
Ontario market liquidity reserve		**(3)**		(7)
Total		**(27)**		(7)

Foreign exchange derivative instruments that are not designated as hedges have a weighted average exchange rate of U.S. $0.85.

Fair Value of Other Financial Instruments

The carrying values of cash and cash equivalents, accounts receivable, accounts payable and accrued charges, Market Power Mitigation Agreement rebate payable, short-term notes payable, and long-term debt due within one year approximate their fair values due to the immediate or short-term maturity of these financial instruments. Fair values for other financial instruments have been estimated by reference to quoted market prices for actual or similar instruments where available.

The carrying values and fair values of these other financial instruments are as follows:

(millions of dollars)	**Carrying Value** 2005	**Fair Value** 2005	Carrying Value 2004	Fair Value 2004
Financial Assets				
Nuclear fixed asset removal and nuclear waste management funds	**6,788**	**6,788**	5,976	6,000
Long-term accounts receivable and other assets	**61**	**61**	56	56
Financial Liabilities				
Long-term debt	**3,895**	**4,081**	3,404	3,582
Long-term accounts payable and accrued charges	**183**	**183**	212	212

Credit Risk

Credit risk is the financial risk of non-performance by contractual counterparties. Credit risk excludes any operational risk resulting from a third party failing to deliver a product or service as expected. OPG derives revenue from several other sources including the sale of energy products and financial risk management products to third parties. However, the majority of OPG revenues are derived from sales through the IESO administered spot market.

Credit exposure to the IESO fluctuates based on spot prices and the volume of rate regulated and unregulated generation, and is reduced each month upon settlement of the accounts. Credit exposure to the IESO peaked at $1,146 million during the year ended December 31, 2005 and at $901 million during the year ended December 31, 2004.

13 Common Shares

As at December 31, 2005 and 2004, OPG had 256,300,010 common shares issued and outstanding at a stated value of $5,126 million. OPG is authorized to issue an unlimited number of common shares without nominal or par value.

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. OPG had become aware of a class action suit for $50 billion, relating to alleged negative health impacts caused by burning coal to generate electricity, that has been issued in an Ontario Court naming OPG and 20 U.S.-based electricity generators as defendants. Although the claim was filed in the court office, it has not been served on OPG and, the time allowed to the plaintiff to serve the claim has expired. While the court has discretion to extend the time for service upon a motion by the Plaintiffs, OPG does not believe this is likely. The preliminary assessment is that the claim would be unlikely to succeed even if the Plaintiffs further pursued the claim.

In July 2004, OPG and two individual OPG employees were each charged with criminal negligence causing death and criminal negligence causing bodily harm in relation to a 2002 drowning accident at Barrett Chute. The trial commenced on January 16, 2006, and is expected to last approximately four to six months.

Also, certain First Nations have commenced actions for interference with reserve and traditional land rights. The claims by some of these First Nations total approximately $50 million and claims by others are for unspecified amounts.

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

Environmental

OPG was required to assume certain environmental obligations from Ontario Hydro. A provision of $76 million was established as at April 1, 1999 for such obligations. During the year ended December 31, 2005, expenditures of $4 million (2004 – $2 million) were recorded against the provision.

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

Guarantees

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

Contractual and Commercial Commitments

The Company's contractual obligations and other significant commercial commitments as at December 31, 2005 are as follows:

(millions of dollars)	2006	2007	2008	2009	2010	Thereafter	Total
Contractual obligations:							
Fuel supply agreements	693	425	197	68	15	15	1,413
Contributions under ONFA	454	454	679	350	350	1,403	3,690
Long-term debt repayment	800	400	400	350	970	775	3,695
Interest on long-term debt	214	168	145	122	90	55	794
Unconditional purchase obligations	26	20	12	9	15	27	109
Long-term accounts payable	28	28	9	–	–	–	65
Operating lease obligations	13	13	13	13	14	–	66
Pension contributions[1]	254	–	–	–	–	–	254
Other	75	34	35	34	35	11	224
Significant commercial commitments:							
Niagara Tunnel	158	173	172	116	1	–	620
Total	2,715	1,715	1,662	1,062	1,490	2,286	10,930

1. The pension contributions include additional funding requirements towards the deficit and ongoing funding requirements in accordance with the actuarial valuation as at January 1, 2005. The contributions are affected by various factors including market performance, changes in actuarial assumptions, plan experience, and the timing of funding valuations. Funding requirements after 2006 are excluded due to significant variability in the assumptions required to project the timing of future cash flows.

In June 2004, OPG announced and the Government of Ontario ("Government") endorsed the decision to proceed with a new water diversion tunnel that will increase the amount of water flowing to existing turbines at the Sir Adam Beck generating stations in Niagara. This tunnel will allow the Beck generating facilities to utilize available water more effectively, and is expected to increase annual generation on average by about 1.6 TWh. OPG awarded a contract to Strabag AG in August 2005 to design and construct the 10.4 kilometre tunnel and associated facilities. The value of the design-build contract is approximately $600 million, with the total project expected to cost approximately $985 million. Construction started in September 2005. Project completion is expected by late 2009.

Other Commitments
In addition to the above commitments, the Company has the following commitments:

The Company maintains labour agreements with the Power Workers' Union ("PWU"). The agreement is effective from April 1, 2002 to March 31, 2006. OPG and the PWU recently reached tentative agreements, which are subject to membership ratification. The Company also maintains a labour agreement with the Society of Energy Professionals. The agreement is effective from January 1, 2005 to December 31, 2005. The agreement has since been renewed and extended to December 31, 2010. As of December 31, 2005, the Company had approximately 90 per cent of its regular labour forces covered by collective bargaining agreements.

Contractual and commercial commitments above exclude certain purchase orders as they represent purchase authorizations rather than legally binding contracts and are subject to change without significant penalties.

Proxy Property Taxes
In November 2005, OPG received a letter from the Ministry of Finance indicating its intent to recommend to the Minister of Finance that an Ontario regulation covering proxy property taxes be updated retroactive to April 1, 1999 to reflect reassessments and appeal settlements of certain OPG properties since that date. Updates to the regulation may not occur for up to two years. OPG has not recorded any amounts relating to this anticipated regulation change.

15 Restructuring

The change in the restructuring liability for termination benefits for 2005 and 2004 is as follows:

(millions of dollars)	**2005**	2004
Liability, beginning of year	**20**	52
Restructuring charges	**10**	19
Payments	**(18)**	(51)
Liability, end of year	**12**	20

During 2004, OPG recorded restructuring charges of $16 million, which consisted of $15 million for termination benefits and $1 million in related pension and OPEB expenses associated with its Lakeview generating station. OPG also recorded restructuring charges of $4 million related to its Energy Marketing business during 2004. During 2005, OPG recorded restructuring charges of $10 million which consisted of $4 million related to the Lakeview generating station and $6 million related to the Energy Markets business.

16 Transition Rate Option Contracts

Under regulation known as Transition – Generation Corporation Designated Rate Options ("TRO"), OPG has been required to provide transitional price relief since market opening to certain power customers for up to four years based on the consumption and average price paid by each customer during a reference period of July 1, 1999 to June 30, 2000. The TRO is treated as a hedge of generation revenue. The maximum anticipated volume subject to the transitional price relief was approximately 5.4 TWh in the first year after market opening and 3.6 TWh in the second year. The maximum anticipated volume in each of the third and fourth years is 1.8 TWh. The maximum length of the program is four years, which expires April 30, 2006.

A provision of $210 million on the TRO contracts was recorded in the first quarter of 2002 based on the estimated future loss on these contracts. The provision was determined at that time using management's best estimates of the forward price curve for electricity, wholesale electricity market fees, impact of decontrol on these contracts, interruptions of volume, and the recovery of Market Power Mitigation Agreement rebates. The provision for the TRO contracts was established based on meeting decontrol targets within three years of market opening. An additional charge of $30 million related to the fourth year of the TRO contracts was recorded in 2003, based on OPG's expectation that the Company would not meet the decontrol targets necessary for TRO contracts to expire after three years.

The change in the TRO contracts provision for the years ended December 31, 2005 and 2004 is as follows:

(millions of dollars)	**2005**	2004
Provision, beginning of year	**48**	100
Decrease of provision during the year	**(36)**	(52)
Provision, end of year	**12**	48

17 Market Power Mitigation Agreement Rebate

Until April 1, 2005, OPG was required under its generating licence to comply with prescribed market power mitigation measures to address the potential for OPG to exercise market power in Ontario. The market power mitigation measures included both a rebate mechanism and the requirement to decontrol generating capacity. Under the rebate mechanism, a majority of OPG's expected energy sales in Ontario were subject to an average annual revenue cap of 3.8¢/kWh. During the term of the Market Power Mitigation Agreement, OPG was required to pay a rebate to the Independent Electricity System Operator equal to the excess, if any, of the average hourly spot energy price over 3.8¢/kWh for a 12-month settlement period, multiplied by the amount of energy subject to the rebate mechanism. The Market Power Mitigation Agreement was replaced effective April 1, 2005 by a regulated price for baseload hydroelectric and nuclear generation and a revenue limit that applies to OPG's unregulated generation assets.

In accordance with the Market Power Mitigation Agreement, the rebate was calculated after taking into account the amount of energy sales subject to the rebate mechanism for only those generating stations that OPG continues to control. Since the average hourly spot price during the three months ended March 31, 2005, when the rebate mechanism ended, exceeded the 3.8¢/kWh revenue cap, OPG provided $412 million (2004 – $1,154 million) as a Market Power Mitigation Agreement rebate.

The change in the Market Power Mitigation Agreement rebate liability for the years ended December 31, 2005 and 2004 is as follows:

(millions of dollars)	**2005**	2004
Liability, beginning of year	**439**	409
Increase to provision during the year	**412**	1,154
Payments	**(851)**	(1,124)
Liability, end of year	**–**	439

18 Revenue Limit Rebate

Eighty-five per cent of the generation output from OPG's unregulated generation assets, excluding the Lennox generating station, TRO volumes and forward sales as of January 1, 2005, is subject to a revenue limit based on an average price of $47.00/MWh (4.7¢/kWh). This revenue limit was originally established for a period of 13 months ending April 30, 2006. The Government has recently announced the extension of the revenue limit for an additional three years. Starting May 1, 2006, the revenue limit will decrease to 4.6¢/kWh from the present limit of 4.7¢/kWh. On April 1, 2007, the revenue limit will return to 4.7¢/kWh and increase to 4.8¢/kWh effective April 1, 2008. Revenues above these limits will be returned to the Independent Electricity System Operator ("IESO"), and the IESO will subsequently issue a rebate to consumers.

The change in the revenue limit rebate liability for the year ended December 31, 2005 is as follows:

(millions of dollars)	**2005**
Liability, beginning of year	**–**
Increase to provision during the year	**739**
Payments	**–**
Liability, end of year	**739**

19 Business Segments

A regulation made pursuant to the Electricity Restructuring Act, 2004 provided that OPG would receive regulated prices for its baseload hydroelectric and nuclear facilities. These initial prices took effect April 1, 2005, and are expected to remain in effect until at least March 31, 2008, at which time it is anticipated that the OEB will have established new regulated prices. Given the effective date of these prices, and OPG's management approach, OPG changed its definition of business segments on April 1, 2005 from Generation and Energy Marketing to Regulated – Nuclear, Regulated – Hydroelectric and Unregulated Generation. OPG will continue to report other activities, including the previously separately presented trading activities in the Other category. As a result of this change in definition, OPG has reclassified the comparative periods to be consistent with the current presentation of business segments.

Regulated – Nuclear Segment

OPG's Regulated – Nuclear business segment operates in Ontario, generating and selling electricity from the nuclear generating stations that it owns and operates. The business segment includes electricity generated by the Pickering A and B, and Darlington nuclear generating stations.

OPG's Regulated – Nuclear business segment includes revenue under the terms of a lease arrangement with Bruce Power related to the Bruce nuclear generating stations. The arrangement includes lease revenue, interest income and revenue from engineering analysis and design, technical and other services. The Regulated – Nuclear business segment also includes revenue earned from isotope sales and ancillary services. Ancillary revenues are earned through voltage control/reactive support. These earnings are included in the Regulated – Nuclear business segment since they were included in determining the regulated price for production from the nuclear facilities.

Bruce Nuclear Generating Stations

In May 2001, the Company leased its Bruce A and Bruce B nuclear generating stations to Bruce Power until 2018, with options to renew for up to 25 years.

Under the terms of the lease, OPG agreed to transfer certain fuel and material inventory to Bruce Power, in addition to certain fixed assets. Pension assets and liabilities related to the approximately 3,000 employees were transferred to Bruce Power. Bruce Power assumed the liability for other post employment benefits for these employees. OPG makes payments to Bruce Power in respect of other post employment benefits of approximately $2.3 million per month over a 72-month period, ending in 2008.

As part of the closing, OPG recorded deferred revenue to reflect the initial payments of $595 million less net assets transferred to Bruce Power under the lease agreement. The deferred revenue is being amortized over the initial lease term of approximately 18 years and is recorded as revenue.

In December 2002, British Energy plc, entered into an agreement to dispose of its entire 82.4 per cent interest in Bruce Power. The transaction was completed in February 2003 and a consortium of Canadian companies assumed the lease of the Bruce A and Bruce B nuclear generating stations that was formerly held by British Energy plc. The Bruce facilities will continue to be operated by Bruce Power. Upon closing of the transaction, the $225 million note receivable was paid to OPG, and lease payments commenced to be paid monthly. Proceeds from the note are to be applied by March 2008 against OPG's funding requirements with respect to the nuclear fixed asset removal and nuclear waste management liabilities.

As part of the agreement reached in October 2005 between the Province and Bruce Power, OPG received a Shareholder Declaration from the Province instructing OPG's Board of Directors to accept certain amendments to the lease agreement. These amendments included a change to the provisions regarding the transfer of Bruce Power's interest in the site and included a reduction of the annual lease payment for three of the four refurbished Bruce A units to $5.5 million per unit (in 2002 dollars, escalated at CPI), after the planned future refurbishments are completed. These changes to the lease agreement will impact OPG when Units 1 and 2 of the Bruce A nuclear generating station are returned to service, and when Unit 3 is refurbished at the end of its current operational life. Other changes to the existing arrangements were made to address Cameco Corporation's decision not to participate in the refurbishment of the Bruce A nuclear generating station.

For 2004 through 2008, minimum payments under the lease are $190 million annually, subject to limited exceptions. The lease revenue of $244 million (2004 – $236 million) was recorded in revenue. The remaining terms of the operating lease agreement will remain substantially unchanged until the planned future refurbishments are completed.

The net book value of fixed assets on lease to Bruce power including costs relating to refurbishing and restarting Bruce A at December 31, 2005, was $492 million (2004 – $590 million).

Regulated – Hydroelectric Segment

OPG's Regulated – Hydroelectric business segment operates in Ontario, generating and selling electricity from its baseload hydroelectric generating stations. The business segment includes electricity generated by the Sir Adam Beck 1, 2 and Pump generating station, DeCew Falls 1 and 2, and the R.H. Saunders hydroelectric facilities. The Regulated – Hydroelectric business segment also includes ancillary revenues related to these stations earned through offering available generating capacity as operating reserve and through the supply of other ancillary services including voltage control/reactive support, certified black start facilities and automatic generation control.

Unregulated Generation Segment

OPG's Unregulated Generation business segment operates in Ontario, generating and selling electricity from its fossil-fuelled generating stations and from the hydroelectric generating stations not included in the Regulated – Hydroelectric segment. The Unregulated Generation business segment also includes ancillary revenues earned through offering available generating capacity as operating reserve, and through the supply of other ancillary services including voltage control/reactive support, certified black start facilities and automatic generation control, and revenues from other services.

Other

OPG earns revenue from its joint venture share of the Brighton Beach Power Limited Partnership ("Brighton Beach") related to an energy conversion agreement between Brighton Beach and Coral Energy Canada Inc. ("Coral"). In addition, the Other category includes revenue from real estate rentals.

The revenue and expenses related to OPG's trading and other non-hedging activities are also included in the Other category. As part of these activities, OPG transacts with counterparties in Ontario and neighbouring energy markets in predominantly short-term trading activities of typically one year or less in duration. These activities relate primarily to physical energy that is purchased and sold at the Ontario border, sales of financial risk management products and sales of energy-related products. All contracts that are not designated as hedges are recorded as assets or liabilities at fair value, with changes in fair value recorded in other revenue as gains or losses.

Segment Income for year ended December 31, 2005	Regulated – Nuclear	Regulated – Hydroelectric	Unregulated Generation	Other	Total
(millions of dollars)					
Revenues					
Revenue	2,607	857	3,399	86	6,949
Market Power Mitigation Agreement rebate	(160)	(65)	(187)	–	(412)
Revenue limit rebate	–	–	(739)	–	(739)
	2,447	792	2,473	86	5,798
Fuel expense	115	254	928	–	1,297
Gross margin	2,332	538	1,545	86	4,501
Operations, maintenance and administration	1,788	77	594	57	2,516
Depreciation and amortization	374	68	276	35	753
Accretion on fixed asset removal and nuclear waste management liabilities	467	–	9	–	476
Earnings on nuclear fixed asset removal and nuclear waste management funds	(381)	–	–	–	(381)
Property and capital taxes	31	18	54	4	107
Restructuring	–	–	4	6	10
Income (loss) before the following:	53	375	608	(16)	1,020
Impairment of long-lived assets	63	–	202	–	265
(Loss) income before interest, income taxes and extraordinary item	(10)	375	406	(16)	755

Segment Income for year ended December 31, 2004	Regulated – Nuclear	Regulated – Hydroelectric	Unregulated Generation	Other	Total
(millions of dollars)					
Revenues					
Revenue	2,421	1,018	2,528	105	6,072
Market Power Mitigation Agreement rebate	(374)	(194)	(586)	–	(1,154)
Revenue limit rebate	–	–	–	–	–
	2,047	824	1,942	105	4,918
Fuel expense	108	255	790	–	1,153
Gross margin	1,939	569	1,152	105	3,765
Operations, maintenance and administration excluding Pickering A return to service	1,611	74	576	62	2,323
Pickering A return to service	271	–	–	–	271
Depreciation and amortization	360	71	302	32	765
Accretion on fixed asset removal and nuclear waste management liabilities	445	–	8	–	453
Earnings on nuclear fixed asset removal and nuclear waste management funds	(313)	–	–	–	(313)
Property and capital taxes	33	18	38	14	103
Restructuring	–	–	16	4	20
Other income	–	–	–	(8)	(8)
(Loss) income before interest, and income taxes	(468)	406	212	1	151

(millions of dollars)	Regulated – Nuclear	Regulated – Hydroelectric	Unregulated Generation	Other	Total
Selected Balance Sheet Information					
December 31, 2005					
Segment property, plant and equipment, net	**3,156**	**4,054**	**3,607**	**595**	**11,412**
December 31, 2004					
Segment property, plant and equipment, net	3,305	4,015	3,986	634	11,940
Selected Cash Flow Information					
Year ended December 31, 2005					
Capital expenditures	**273**	**101**	**90**	**34**	**498**
Year ended December 31, 2004					
Capital expenditures	365	25	78	93	561

20 Related Party Transactions

Given that the Province owns all of the shares of OPG, related parties include the Province, the other successor entities of Ontario Hydro, including Hydro One Inc. ("Hydro One"), the IESO, and the OEFC. OPG also enters into related party transactions with its joint ventures. The transactions between OPG and related parties are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

These transactions are summarized below:

(millions of dollars)	**Revenues**	**Expenses**	Revenues	Expenses
	2005		2004	
Hydro One				
Electricity sales	**40**	**–**	40	–
Services	**–**	**12**	–	12
Settlement Transactions	**–**	**27**	–	33
Province of Ontario				
GRC water rentals and land tax	**–**	**132**	–	152
Guarantee fee	**–**	**8**	–	8
Used Fuel Fund rate of return guarantee	**–**	**–**	–	14
Decommissioning Fund excess funding	**–**	**7**	–	–
Other	**–**	**–**	–	2
OEFC				
GRC and proxy property tax	**–**	**207**	–	214
Interest income on receivable	**–**	**(75)**	–	(101)
Interest expense on long-term notes	**–**	**211**	–	191
Capital tax	**–**	**51**	–	49
Income taxes	**–**	**192**	–	(80)
Indemnity fees	**–**	**5**	–	5
IESO				
Electricity sales	**6,517**	**329**	5,465	304
Market Power Mitigation Agreement rebate	**(412)**	**–**	(1,154)	–
Revenue limit rebate	**(739)**	**–**	–	–
Ancillary services	**68**	**–**	90	–
Other	**–**	**–**	1	1
	5,474	**1,106**	4,442	804

At December 31, 2005, accounts receivable included $14 million (2004 – $14 million) due from Hydro One and $324 million (2004 – $158 million) due from the IESO. Accounts payable and accrued charges at December 31, 2005 included $2 million (2004 – $3 million) due to Hydro One.

21 Joint ventures

Significant joint ventures include Brighton Beach Power L.P., which is 50 per cent owned by OPG (2004 – 50 per cent).

The following condensed information from the consolidated statements of operations, cash flows and balance sheets detail the Company's share of its investment in joint ventures and partnerships that have been proportionately consolidated:

(millions of dollars)	**2005**	2004
Proportionate joint venture operations		
Operating revenue	**46**	28
Operating expenses	**(36)**	(22)
Net income	**10**	6
Proportionate joint venture cash flows		
Operating activities	**21**	4
Investing activities	**(2)**	(34)
Financing activities	**(4)**	32
Share of increase in cash	**15**	2
Proportionate joint venture balance sheets		
Current assets	**26**	16
Long-term assets	**279**	286
Current liabilities	**(11)**	(5)
Long-term liabilities	**(199)**	(202)
Share of net assets	**95**	95

22 Investment Company

The Company applied AcG-18 for all investments owned by OPGV in 2005. OPGV is a wholly owned subsidiary of the Company and its results are consolidated into the Company's financial statements. Since OPGV is the only enterprise in the group that satisfies the criteria set out in AcG-18, all other investments made by OPG and its subsidiaries, partnerships or joint ventures continue to be carried at amortized cost. The carrying amount of OPGV's investments was $29 million (2004 – $36 million) and the amount was included as long-term accounts receivable and other assets on the consolidated balance sheets.

As a result of the application of this policy, the Company's net income for 2005 decreased by $11 million and other assets decreased by the same amount. The gross unrealized gains and losses on the investment held by OPGV as at December 31, 2005 were $2 million and $13 million respectively.

23 Research and Development

For the year ended December 31, 2005, $19 million (2004 – $21 million) of research and development expenses were charged to operations.

24 Other Income

There was no other income recorded in 2005. Other income of $8 million in 2004 was comprised of $3 million from the sale of assets and $5 million from a favourable pension liability settlement.

25 Changes in Non-Cash Working Capital Balances

(millions of dollars)	**2005**	2004
Accounts receivable	**(191)**	(15)
Income taxes recoverable	**–**	16
Fuel inventory	**(12)**	(45)
Materials and supplies	**(23)**	(19)
Market Power Mitigation Agreement rebate payable	**(439)**	30
Revenue limit rebate payable	**739**	–
Accounts payable and accrued charges	**10**	(78)
Income and capital taxes payable	**69**	12
	153	(99)

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Jim Hankinson

President and CEO

Donald Hintz

Retired President,
Entergy Corporation

Gary Kugler

Corporate Director

M. George Lewis

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RBC Asset
Management Inc.

David J. MacMillan

Corporate Director

Corbin A. McNeill Jr.

Retired Chairman and
Co-Chief Executive Officer,
Exelon Corporation

Peggy Mulligan

Executive Vice
President and Chief
Financial Officer,
Linamar Corporation

C. Ian Ross

Chairman,
GrowthWorks Canadian
Fund Ltd.

Marie C. Rounding

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Gowling Lafleur
Henderson LLP

William (Bill) Sheffield

Corporate Director

David G. Unruh

Corporate Director

*Titles of Board directors are current as of May 2006

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Jim Hankinson

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Bruce Boland

Senior Vice President, Corporate Affairs


Jim Burpee

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Pierre Charlebois

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Cara Clairman

Acting Vice President, Law and General Counsel; Acting Vice President, Sustainable Development


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Senior Vice President and Chief Financial Officer


Catriona King

Vice President, Corporate Secretary


John Murphy

Executive Vice President, Hydro


Colleen Sidford

Vice President, Treasurer


Jim Twomey

Executive Vice President, Fossil

*Titles of officers are current as of May 2006

Ontario Power Generation Facilities

3 nuclear stations

5 fossil-fuelled stations

64 hydroelectric stations

3 wind power stations (includes OPG's 50% interest in the Huron Wind joint venture)

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ONTARIO POWER GENERATION