



MANAGEMENT'S DISCUSSION AND ANALYSIS

For the year ended December 31, 2006

(amounts in thousands of dollars unless otherwise noted)

This discussion contains forward looking statements that are subject to risks, uncertainties and assumptions. These statements reflect the current views of management based on information available as at the date of this report. Management does not intend to update this information and disclaims any legal obligation for actual results that vary from those implied by forward looking statements.

The following discussion and analysis should be read in conjunction with the consolidated financial statements and Auditor's Report included in this annual report and any reference to financial statements or related note disclosures in this document refer to the consolidated financial statements and notes. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles.

OVERVIEW

Hamilton Utilities Corporation (the "Corporation") is a multi-utility holding company with investments primarily in regulated utilities that deliver related services to its customers. The Corporation was established in response to the restructuring and deregulation of Ontario's electricity industry, pursuant to the *Energy Competition Act (Ontario), 1998* (the "ECA"), which is presently regulated by the Ontario Energy Board (the "OEB"), a board appointed by the Lieutenant Governor in Council of the Province of Ontario (the "Province"). The sole shareholder of the Corporation is the City of Hamilton.

The Corporation's principal operating subsidiary Horizon Utilities Corporation ("Horizon Utilities") is an electricity distributor for businesses and residents within the City of Hamilton and the City of St. Catharines, the activities of which are regulated by the OEB. Horizon Utilities also provides certain non-regulated water billing and customer care services to the City of Hamilton. On March 1, 2005, the former Hamilton Hydro Inc. ("HHI"), a regulated electricity distribution company then wholly-owned by the Corporation, merged with St. Catharines Hydro Utility Services Inc. ("SCHUSI"), also a regulated distribution company then wholly-owned by St. Catharines Hydro Inc. ("SCHI"), by amalgamation under the *Business Corporations Act (Ontario)* and continue as Horizon Utilities Corporation. Horizon Utilities is 78.9% owned by the Corporation and 21.1% owned by St. Catharines Hydro Inc.

The ECA and its enabling statutes and regulations distinguish and require the separation of regulated electricity businesses from non-regulated business activities. The consolidated financial statements include results for both the regulated and non-regulated business activities of its subsidiaries.

The other non-regulated utility businesses of the Corporation are operated through its wholly-owned subsidiary, Hamilton Hydro Services Inc.:

- FibreWired is a telecommunications services business which charges a broad range of business and institutional customers for the use of its fibre-optic network and provides a range of related services to the same.
- Hamilton Community Energy (HCE), through a district energy system, generates and distributes heat and electricity to commercial and institutional customers within the downtown core of Hamilton under long-term contracts.

Electricity distribution

The electricity distribution business of the Corporation represented approximately 91% (2005 – 92%) of consolidated assets and 89% (2005 - 89%) of consolidated revenue and other income at year end. This business distributes electricity through approximately 3,300 kilometres of a low-voltage distribution system



to approximately 232,000 residential and business customers. The distribution system serves all residents and businesses within the borders of Hamilton and St. Catharines with the exception of approximately 25,000 rural customers served by another electricity distributor.

The Corporation earns revenue from this business by charging its customers for the use of the distribution system. Such electricity distribution services charges, or distribution charges, comprise a fixed periodic service charge combined with a variable charge based on electricity consumption. The distribution charges are subject to the approval of the provincial industry regulator, the OEB.

Pursuant to industry regulation, the Corporation is required to be the default billing and collecting agent for all electricity related charges for all electricity industry participants, which, in addition to its own distribution charges, include transmission charges accruing to the provincially owned Hydro One Inc., commodity costs for electricity accruing to generators such as the provincially owned Ontario Power Generation Inc. ("OPGI"), service charges for market participants such as the Independent Electricity System Operator ("IESO"), and the "Debt Retirement Charge" which is a provincial charge directed to the repayment of certain debt obligations of the former Ontario Hydro which continue in the provincially owned Ontario Electricity Financial Corporation ("OEF"), an agency of the Ontario government. These other non-distribution charges represent "pass-through" charges accruing to these and other electricity industry participants and amounted to approximately 85% (2005 - 86%) of gross annual amounts billed by the Corporation. The Corporation must remit these non-distribution charges to other industry participants, irrespective of whether or not such charges are ultimately collected from customers, thus exposing the Corporation to credit risk well in excess of its own capacity to generate revenue. The Corporation has instituted credit policy to mitigate such risk.

Electricity Regulation

The Ontario Energy Board Act, 1998 (Ontario) ("OEBA") conferred on the Ontario Energy Board ("OEB") increased powers and responsibilities to regulate the electricity industry in Ontario. These powers and responsibilities include approving or fixing rates for the transmission and distribution of electricity, providing continued rate protection for rural and remote electricity consumers, and ensuring that distribution companies fulfill obligations to connect and service customers. The OEB may also prescribe license requirements and conditions of service to electricity distributors which may include, among other things, record keeping, regulatory accounting principles, separation of accounts for distinct businesses, and filing and process requirements for rate setting purposes.

Rate Setting

The Company's distribution rates are based on a revenue requirement that provides a regulated rate of return on the amount of shareholder's equity supporting the business of electricity distribution. Distribution rates for 2005 were based on an annual rate of return of 9.88% on the amount of common equity deemed to be allocated to this business, presently regulated at 40% of the Corporation's investment in electricity distribution assets and related working capital requirements. As mandated by the OEB, the rate increase in 2005 was subject to a financial commitment by the Corporation to invest \$7,071 in conservation and demand management activities over the period September 1, 2005 to September 30, 2007.

On April 12, 2006, the OEB approved the Corporation's Electricity Distribution Rate Application for 2006 distribution rates, for rates to be effective May 1, 2006. The 2006 distribution rate, in accordance with the OEB filing requirements, provides for a revised rate of return of 9.0%, as compared to 9.88% in previous years.

In accordance with the OEB Report on Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors, distribution rates for 2007 will be established based on an OEB approved incentive regulation mechanism model ("the IRM Model"). The IRM Model adjusts 2007 distribution rates by increasing them for the 2006 Canada Gross Domestic Product Implicit Price Index less a Productivity Factor of 1% as determined by the OEB, or 0.92% for 2007 effective May 1st.



Regulatory Accounting

In its capacity to approve or set rates, the OEB has the authority to specify regulatory accounting treatments that may differ from Canadian generally accepted accounting principles for enterprises operating in a non-rate regulated environment. The OEB has the general power to include or exclude costs, revenues, losses or gains in the rates of a specific period, resulting in a change in the timing of accounting recognition from that which would have applied in an unregulated company. Such change in timing involves the application of rate regulated accounting, giving rise to the recognition of regulatory assets and liabilities. The Corporation's regulatory assets represent certain amounts receivable from customers in the future and costs that have been deferred for accounting purposes because it is probable that they will be recovered in future rates. The Corporation's regulatory liabilities represent costs with respect to non-distribution market related charges and variances in recoveries that are expected to be settled in future periods.

The Electricity Restructuring Act (Ontario), 2004 (the "ERA")

On December 9, 2004, the Province enacted the ERA, which provides for a restructuring of Ontario's electricity sector to promote the expansion of electricity supply and capacity, alternative and renewable energy sources, and conservation and demand management. Under the ERA, the commodity cost of electricity for certain customer classes will be determined by the OEB on an annual basis and based on a combination of regulated, contract and competitive market prices for electricity. There are few provisions in the ERA that apply to electricity distributors.

Smart Meter Initiative

The Province of Ontario has committed to have "Smart Meter" electricity meters installed in 800,000 homes and small businesses by the end of 2007 and throughout Ontario by the end of 2010. Smart Meters permit consumption to be recorded within specific time intervals and specific tariffs to be levied within such intervals. *Bill 21, Energy Conservation and Responsibility Act*, provides the legislative framework and regulations to support this initiative.

The estimated total investment by the Corporation through to 2010 is \$35,000 - \$40,000. Such investment is anticipated to be supported by adjustments to electricity distribution rates. The 2006 EDR application of the Corporation provided for a modest initial investment in Smart Meters of \$0.39 per metered customer per month. On January 29, 2007, the OEB issued a Report of the Board on 2nd Generation Incentive Regulation for Ontario's Electricity Distributors – Addendum for Smart Metering Rates, which provides a mechanism for electricity distributors to file for a new smart metering "rate adder" for 2007. The Corporation filed its application for an amendment to its smart meter rate adder on February 9, 2007 requesting a new rate of \$0.82 per meter. The purpose of the rate adder is to provide advanced funding for Smart Meter installations. The approval of Smart Meter implementation costs and future recoveries will be subject to further review by the OEB.

In support of the Smart Meter initiative, the Corporation launched a Smart Meter pilot program in 2006 as part of its conservation and demand management plan approved by the OEB. The primary purpose of the pilot was to develop and test the processes, tools and network infrastructure to support mass deployment in 2007 to 2010.

The Corporation has committed to purchase up to 50,000 Smart Meters and related equipment in 2007. The total financial commitment in 2007 is approximately \$5,500.

Amalgamation of Hamilton Hydro Inc. and St. Catharines Hydro Utility Services Inc.

The amalgamation of HHI and SCHUSI was completed pursuant to a Merger Co-operation Agreement dated November 25, 2004 between the City of Hamilton, as sole shareholder of the Corporation, and The City of St. Catharines, as sole shareholder of St. Catharines Hydro Inc. ("SCHI"), which acknowledged their approval of the merger of HHI and SCHUSI under terms and conditions set out in a Merger Participation Agreement (the "MPA"), dated November 25, 2004, between the Corporation, HHI, SCHI and SCHUSI.



The MPA provided that the respective shareholders of the HHI and SCHUSI, the Corporation and SCHI, receive common shares in Horizon Utilities with votes and value in proportion to the respective values of HHI and SCHUSI.

A valuation of HHI and SCHUSI was undertaken by a competent third party and was largely based on projections of capital assets, capital expenditures and operating expenses anticipated to be permitted by regulation administered by the OEB in its approval of allowable distribution charges for each respective corporation. The values agreed to by HUC and SCHI (the "Parties") were as negotiated by the Parties based on such valuation. The results of the negotiation and valuation provide for common share allocations of 78.9% for the Corporation and 21.1% for SCHI.

This transaction resulted in the Corporation receiving a controlling interest in Horizon Utilities. The transaction was recorded by Horizon Utilities using the purchase method of accounting. As such, the results of operations and cash flow for 2005 reflects that of Horizon Utilities for the ten months ended December 31, 2005 and HHI for the two months ended February 28, 2005.

In accordance with the MPA, immediately prior to the merger, HHI declared a dividend in specie to HUC consisting of the right to receive any future amounts received by Horizon Utilities that represent the recovery of any regulatory assets in excess of HHI's book value of such assets as at February 28, 2005. SCHUSI also declared a dividend in specie to SCHI consisting of the right to receive any future amounts received by Horizon Utilities that represent the recovery of any regulatory assets in excess of SCHUSI's book value of such assets as at February 28, 2005. In April 2006, the OEB approved Horizon Utilities' application for the recovery of regulatory asset balances as at December 31, 2004, resulting in amounts recoverable by the Corporation and SCHI under the MPA of \$2,779 and \$2,935 respectively.

RESULTS OF OPERATIONS

Year Ended December 31, 2006 compared to Year Ended December 31, 2005

As noted previously, the 2005 consolidated results of operations include the results of operations for Horizon Utilities for the ten months ended December 31, 2005 and HHI for the two months ended February 28, 2005.

Net income

Net income for the year was \$16,242 and reflects an increase of \$3,873 or 31.3% increase over 2005 net income of \$12,369. The increase in net income over the prior year primarily reflects strong financial results for the Corporation's electricity distribution business, as well as a pre-tax recovery of \$2,779 with respect to the recovery of regulatory assets.

Electricity distribution operations

Net income for the electricity distribution business was \$11,807 compared to \$10,232 in the prior year. The increase in net income was primarily attributable to higher electricity distribution and other regulated service rate charges as a result of new electricity distribution rates that permit the Corporation to achieve the theoretical regulated rate of return in its electricity distribution operations. Operating expenditures decreased over the prior year and the Corporation remains committed to containing and reducing costs through process improvement and expanding its customer base to achieve economies of scale and scope.

*FibreWired*

Net income for FibreWired was \$985 in 2006 compared to \$1,279 in 2005. Net income in the prior year included a pre-tax gain on sale of assets of \$499, compared to \$70 in the current year. Income from operations remained relatively stable reflecting continued strong performance of its existing product lines but somewhat limited growth opportunities within its current service territory boundaries.

Hamilton Community Energy

Net income for HCE was \$76 in 2006 compared to a net loss of \$703 in 2005. The increase in net income reflects an improvement in operating costs over the prior year, as well as lower interest expense attributable to interest forgiveness on inter-company debt. Although operating results improved in 2006, operations continue to be negatively impacted by unsold thermal capacity and higher than anticipated capital and operating costs. The Corporation is currently undertaking an economic review to develop opportunities for additional thermal sales and cost containment.

Revenues

	<u>2006</u>	<u>2005</u>
<i>Electricity distribution services charges</i>	\$ 79,610	\$ 76,815

Electricity distribution services charges for the year ended December 31, 2006 increased by \$2,795 over the prior year. This increase reflects increases in distribution rates to support the regulated annual rate of return commencing April 1, 2005 and as adjusted May 1, 2006, partially offset by a decrease in electricity consumption due to weather.

	<u>2006</u>	<u>2005</u>
<i>Telecommunications services charges</i>	\$ 8,188	\$ 7,605

Telecommunications services charges for the year ended December 31, 2006 increased by 8% reflecting customer growth in the FibreWired business unit as a result of customer growth in offsite data storage and network access.

	<u>2006</u>	<u>2005</u>
<i>Electricity, heating, and cooling services charges</i>	\$ 2,951	\$ 2,893

These charges represent revenue from the HCE business unit. HCE has long-term contracts with its customers, primarily government and institutional, for the delivery of electricity and heat. The modest increase in these charges primarily reflects increased natural gas volumes to support the delivery of heat to thermal customers, partially offset by lower electricity consumption due to weather.

	<u>2005</u>	<u>2004</u>
<i>Other income from operations</i>	\$ 9,299	\$ 7,339

Other income from operations is comprised primarily of regulated service rate charges to customers, water billing and customer care services provided to the City of Hamilton, late payment charges, rental income from water heaters, sentinel lights and pole attachments, and miscellaneous other income. Other income increased by \$1,960 and primarily reflects increases in regulated service rate charges to customers (\$1,104), an increase in pole attachment rentals to telecommunications and cable television industries (\$412) and sale of scrap (\$379).

Expenses

	<u>2006</u>	<u>2005</u>
<i>Operating expenses</i>	\$ 44,491	\$ 46,037

Operating expenses decreased by \$1,546 in 2006 as compared to 2005.

Electricity Distribution Operations - \$1,555 decrease in 2006

Operating expenses in the prior year included \$2,689 in merger related expenses such as severance costs associated with voluntary retirement and separation programs offered to employees, computer programming, and other administrative costs related to the integration of operations. Excluding the impact of these expenditures from the prior year, operating expenses in 2006 increased by \$1,134 over the prior year, reflecting a full year of operations for Horizon Utilities. The increase in operating expenditures is primarily attributable to expenditures to support regulated conservation and demand management programs (\$694), increased activity in the forestry program (\$484), and increased salaries and benefits to support an investment in skilled trades. These increased costs were partially offset by lower weather related emergency and corrective maintenance costs during the year.

FibreWired – \$636 increase in 2006

This increase is attributable to an increase in staff complement, as well as higher direct costs to support the revenue growth in 2006.

Hamilton Community Energy - \$349 decrease in 2006

This decrease reflects lower salaries and benefits reflecting a reduction in staff, as well as lower average natural gas prices during the year compared to the prior year.

Other –\$278 decrease in 2006

Other includes corporate activities and the elimination of inter-company transactions on consolidation.

	<u>2006</u>	<u>2005</u>
<i>Depreciation and amortization</i>	\$ 22,328	\$ 20,999

The Corporation has applied consistent amortization rates to its capital assets throughout the reporting period.

The increase in depreciation reflects higher capital investments in the electricity distribution business. In 2006, the electricity distribution business invested approximately \$31,426 in capital assets, as compared to approximately \$18,848 in 2005. The increase reflects higher distribution system capital expenditures (\$9,128), expenditures related to regulated conservation and demand management programs (\$1,912) and other capital expenditures (\$1,538), including vehicles, building upgrades, furniture and office equipment. The increase in distribution system capital expenditures reflects an increase in customer demand projects, system reliability projects and the replacement of aging infrastructure. The electricity distribution business operates within a mature and low-growth service area resulting in a predictable capital program that is largely based on routine replacement of aging infrastructure. The average recurring annual capital maintenance program for the electricity distribution business is estimated to be approximately \$25,000 to \$28,000. Additional non-recurring capital investments of approximately \$5,000 are anticipated over the next three years.

The Province of Ontario has committed to have “Smart Meter” electricity meters installed in 800,000 homes and small businesses by the end of 2007 and throughout Ontario by the end of 2010. Smart Meters permit consumption to be recorded within specific time intervals and specific tariffs to be levied within



such intervals. *Bill 21, Energy Conservation and Responsibility Act*, provides the legislative framework and regulations to support this initiative. The estimated total investment by the Corporation through to 2010 is \$35,000 - \$40,000 and is in addition to the aforementioned recurring capital program. Such investment is anticipated to be supported by adjustments to future electricity distribution rates.

In 2006, as part of its conservation and demand management programs, the Corporation launched a Smart Meter pilot program to install 7,500 Smart Meters. The primary purpose of the pilot was to develop and test the processes, tools and network infrastructure to support mass deployment in 2007 to 2010.

	<u>2006</u>	<u>2005</u>
<i>Recovery of qualifying transition costs</i>	\$ 2,779	\$ -

The recovery of qualifying transition costs reflects the recovery of specific and incremental costs incurred by the former HHI for systems and process changes to support the opening of the competitive electricity market in Ontario on May 1, 2002. These costs were previously deferred for regulatory accounting purposes and were subject to review and approval for recovery by the OEB. Given a reasonable doubt of recovery due to the former revenue rate cap imposed by the Government of Ontario, the former HHI had written-off these costs as a charge against income. As previously noted, in accordance with the MPA, the Corporation was entitled to receive any regulatory asset recovery amounts in excess of HHI's book value of such assets as at February 28, 2005. In April 2006, the OEB approved Horizon Utilities' application for the recovery of regulatory asset balances as at December 31, 2004, resulting in amounts recoverable by the Corporation under the MPA of \$2,779.

	<u>2006</u>	<u>2005</u>
<i>Interest income</i>	\$ (1,294)	\$ (1,155)
<i>Interest expense</i>	\$ 8,070	\$ 7,784

The net increase in interest expense over the prior year primarily reflects carrying charges realized on regulatory liabilities, as well as interest paid on increased customer deposit balances. Included in interest expense in the prior year was \$417 in interest paid on a \$29,124 promissory note payable to SCHI that was assumed by the Corporation on the acquisition of SCHUSI on March 1, 2005 and repaid in full on June 17, 2005.

	<u>2006</u>	<u>2005</u>
<i>Payments in lieu of income and large corporations taxes (PILs)</i>	\$ 9,971	\$ 6,920

The Corporation is currently exempt from taxes under the *Income Tax Act (Canada)* and the *Ontario Corporations Tax Act* (collectively referred to as the "Tax Acts").

Commencing October 1, 2001 and pursuant to the ECA, the Corporation is required to compute taxes under the Tax Acts and remit such amounts to OEFC to be applied against certain debt obligations of the former Ontario Hydro continuing in Ontario Electricity Financial Corporation.

The effective rate of PILs expense in 2006 was 33.96% (2005 – 32.04%) versus the statutory rate of 36.12% (2005 – 36.12%). The favourable effective rate primarily reflects a tax basis of depreciable capital property and eligible capital expenditure in excess of the book basis. The tax basis of the Corporation's assets was valued at fair value pursuant to the provisions of the Tax Acts as at the date the Corporation became subject to PILs. Partially offsetting this favourable effective rate was an adjustment to future PILS to reflect an anticipated reduction in the future effective tax rate to 32.5% by 2011 (*refer to Note 6*). The Corporation anticipates favourable effective tax rates on income relative to statutory rates for the next several years.

**Year Ended December 31, 2005 compared to Year Ended December 31, 2004**

As noted previously, the 2005 consolidated results of operations include the results of operations for Horizon Utilities for the ten months ended December 31, 2005 and HHI for the two months ended February 28, 2005. The 2004 comparative consolidated results of operations include the results of operations of HHI.

Revenues

	<u>2005</u>	<u>2004</u>
<i>Electricity distribution services charges</i>	\$ 76,815	\$ 57,036

Electricity distribution services charges for the year ended December 31, 2005 increased by \$19,779 over the prior year. This increase reflects revenue contributed by the former SCHUSI subsequent to the merger on March 1, 2005 (\$15,411), and an increase in weather related electricity consumption (\$4,368).

	<u>2005</u>	<u>2004</u>
<i>Telecommunications services charges</i>	\$ 7,605	\$ 6,714

Telecommunications services charges for the year ended December 31, 2005 increased by 13% reflecting customer growth in the FibreWired business unit as a result of new product offerings such as offsite data storage and wireless connectivity services.

	<u>2005</u>	<u>2004</u>
<i>Electricity, heating, and cooling services charges</i>	\$ 2,893	\$ 2,262

These charges represent revenue from the HCE business unit. HCE has long-term contracts with its customers, primarily government and institutional, for the delivery of electricity and heat. The increase in these charges reflect the addition of a new customer to the district energy system in February 2005, an increase in weather related electricity consumption and pass through of increased natural gas costs to thermal customers.

	<u>2005</u>	<u>2004</u>
<i>Other income from operations</i>	\$ 7,339	\$ 6,019

Other income from operations is comprised primarily of water billing and customer care services provided to the City of Hamilton, late payment charges, rental income from water heaters, sentinel lights and pole attachments, and miscellaneous other income. This increase reflects revenue contributed by the former SCHUSI subsequent to the merger (\$775), as well as increases in water billing charges, water heater rental rates and an increase in the regulated pole attachment rates charged to telecommunications and cable television industries (\$545).

Expenses

	<u>2005</u>	<u>2004</u>
<i>Operating expenses</i>	\$ 46,037	\$ 32,540

Operating expenses increased by \$13,497 in 2005 as compared to 2004.

Electricity Distribution Operations - \$13,272 increase in 2005

This increase is primarily attributable to the contribution by SCHUSI subsequent to the merger on March 1, 2005 (\$8,500). The Corporation also incurred \$2,689 in merger related expenses such as severance costs associated with voluntary retirement and separation programs offered to employees, computer programming, and other administrative costs related to the integration of operations. The merger is



expected to result in annualized net operating and capital costs savings of approximately \$4,800 as a result of the elimination of systems and process redundancies.

Increased activity in the forestry program (\$600), expenditures to support regulated conservation and demand management programs (\$205), and higher credit losses (\$781) also contributed to the increase in operating expenses during 2005. Credit losses in the prior year reflected a pre-tax recovery of \$1,080 related to a credit loss from Stelco Inc., the largest customer of the Corporation, including certain set-offs and proceeds realized from the sale and assignment of a receivable from Stelco Inc. to a third party.

FibreWired – \$348 increase in 2005

This increase is attributable to related revenue growth in 2005.

Hamilton Community Energy - \$631 increase in 2005

This increase reflects price excursions for natural gas and the addition of a new customer to the district energy system.

Other –\$754 decrease in 2005

Other includes corporate activities and the elimination of inter-company transactions on consolidation.

	<u>2005</u>	<u>2004</u>
<i>Depreciation and amortization</i>	\$ 20,999	\$ 17,209

The Corporation has applied consistent amortization rates to its capital assets throughout the reporting period.

The merger of the Corporation with SCHUSI contributed \$3,412 of the \$3,790 increase in depreciation expense for the year.

In 2005, the electricity distribution business invested approximately \$18,848 in capital assets as compared to approximately \$16,129 in 2004. The increase reflects approximately \$1,842 in capital expenditures for the former SCHUSI service territory subsequent to March 1, 2005, as well as capital expenditures related to regulated conservation and demand management programs.

	<u>2005</u>	<u>2004</u>
<i>Interest income</i>	\$ (1,155)	\$ (1,110)
<i>Interest expense</i>	\$ 7,784	\$ 7,343

The net increase in interest income and expense reflects \$417 in interest paid on a \$29,124 promissory note payable to SCHI that was assumed by the Corporation on the acquisition of SCHUSI on March 1, 2005. The promissory note was subsequently repaid in full on June 17, 2005. There were no significant changes to the financing arrangements of the Corporation during 2005.

	<u>2005</u>	<u>2004</u>
<i>Payments in lieu of income and large corporations taxes (PILs)</i>	\$ 6,920	\$ 5,714

The Corporation is currently exempt from taxes under the *Income Tax Act (Canada)* and the *Ontario Corporations Tax Act* (collectively referred to as the “Tax Acts”).

Commencing October 1, 2001 and pursuant to the ECA, the Corporation is required to compute taxes under the Tax Acts and remit such amounts to OEFC to be applied against certain debt obligations of the former Ontario Hydro continuing in Ontario Electricity Financial Corporation.



The effective rate of PILs expense in 2005 was 32.04% (2004 – 34.15%) versus the statutory rate of 36.12% (2004 – 36.12%) before PILs large corporations tax. The favourable effective rate reflects a tax basis of depreciable capital property and eligible capital expenditure in excess of the book basis. The tax basis of the Corporation's assets was valued at fair value pursuant to the provisions of the Tax Acts as at the date the Corporation become subject to PILs. The Corporation anticipates favourable effective tax rates on income relative to statutory rates for the next several years.

LIQUIDITY AND CAPITAL RESOURCES

Requirements for liquidity and capital resources

The Corporation's principal liquidity and capital resource requirements comprise its ongoing commitment to maintain, improve and expand its distribution and other infrastructure assets on a sustainable basis and in accordance with governing statutes and regulations; working capital requirements; the servicing and repayment of debt obligations; and the payment of dividends to its shareholder.

Capital resource requirements

In addition to the capital program of the electricity distribution business noted above, the Corporation requires capital to continue its infrastructure investments in FibreWired and HCE.

During the year, the Corporation invested \$2,156 (2005 - \$1,482) in FibreWired infrastructure, including customer connections. Approximately \$360 in capital expenditures related to the opening of a new data centre to provide disaster recovery, business continuity, and co-location to existing and prospective customers. The recurring capital program for FibreWired is anticipated to be between \$1,700 and \$1,900 per year to support a sustainable network and new customer connections.

Capital expenditures related to HCE were minimal during the year (2005 - \$968), as no new customers were connected to the district energy facility. Capital expenditures in 2005 reflected a new customer connection to the district energy facility. Future capital expenditure levels for HCE will be dependent upon the Corporation's ability to sell the remaining thermal heating capacity of its existing infrastructure. Thereafter, the Corporation does not anticipate any significant recurring capital investment in this discrete district energy project.

Debt servicing requirements

The Corporation has no debt maturities until 2012.

Dividend requirements

The Corporation paid dividends in the amount of \$5,016 in 2006 to its sole shareholder, compared to \$23,088 paid in 2005. Dividends paid in 2005 included a one-time dividend payment of \$16,605 as result of an adjustment to the capital structure of Horizon Utilities representing retained earnings not required to support the existing business or approved business strategy.

Dividends on common shares are declared at the discretion of the Board of Directors, based on its approved dividend policy and recommendations of management, with consideration for results of operations, financial condition and future outlook, cash requirements and industry practice.

Sources of liquidity and capital resources

The principal sources of liquidity and capital resources comprise funds generated from both operations and financing through the debt capital markets and available bank lines of credit.

*Funds generated from operating activities*

Cash provided from operations was \$24,881 in 2006, as compared to \$60,788 in 2005. The decrease was primarily due a decrease in working capital, including timing differences between collections realized from customer receivables, amounts paid to third-parties with respect to non-distribution charges and decreases in accounts payable. Also reflected in the prior year was the receipt of \$21,463 from the IESO in December 2005 to fund the Ontario Pricing Credit, a refund to residential and small business electricity customers, schools, hospitals and other customers covered by the Regulated Pricing Plan, that sets out prices per kWh that local electricity utilities charge for electricity use. The credits were applied to customer accounts in early 2006.

Financing activities

Short-term and long-term liquidity was available to the Corporation throughout the year through its \$100,000 (2005 - \$93,500) credit facility (*refer to Note 14*). Pursuant to a Second Amended and Restated Credit Agreement (“Credit Facility”) dated January 20, 2006 with a Canadian chartered bank, the Corporation can borrow up to \$100,000 to finance general corporate requirements, working capital requirements and prudential obligations. The amended credit facility expires on January 19, 2009.

Long-term liquidity is available to the Corporation through its access to the debt capital markets by issuing debentures as provided for under its trust indenture (*refer to Note 8*).

The Corporation currently has a credit rating with Standard & Poor’s Rating Services Inc. (“S&P”) of A with a stable outlook. Such was last affirmed November 2, 2006.

RISK FACTORS

The Audit and Risk Management Committee of the Board of Directors is mandated to identify the principal control risks in the business of the Corporation and to verify that effective control systems are in place to manage and mitigate these risks. The President and Chief Executive Officer has ultimate accountability for risk management and the Senior Vice-President and Chief Financial Officer is responsible to the President and Chief Executive Officer for the ongoing monitoring and review of the risk profile, policies and practices of the Corporation and ensuring that the risk management program is an integral part of business strategy and planning.

Significant risk factors affecting the businesses of the Corporation include:

Regulatory risk related to the electricity distribution business

Regulatory risk is the risk that the Province and its regulator, the OEB, could establish a regulatory regime that imposes conditions that restrict the electricity distribution business from achieving an acceptable rate of return that permits financial sustainability of its operations including the recovery of expenses incurred for the benefit of other market participants in the electricity industry such as transition costs and other regulatory assets. All requests for changes in electricity distribution charges require the approval of the OEB.

Credit Risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss.

The principal source of credit risk for the Corporation relates to the realization of its customer receivables. The Corporation earns its revenue from a broad base of customers located in the City of Hamilton and the City of St. Catharines. Two customers account for 6% and 1% of total revenue (2005 – 6% and 1%), one of which is the City of Hamilton, and the other a local school board. No other single customer in either year would account for revenue in excess of 1%.



One customer, the City of Hamilton, accounts for 3.7% of accounts receivable at year-end. No other single customer accounts for more than 1% of accounts receivable at year-end.

Management actively monitors and manages its exposure to credit risk, within regulatory constraints, and records credit losses in the period in which, in management's opinion, the collection of related receivables becomes doubtful.

Regulated electricity distribution business

The legislation governing the operation of Ontario's electricity industry exposes the Corporation, through its electricity distribution operations, to credit risk of several multiples of its means to generate revenue (*refer to Note 15*). Pursuant to Provincial regulation, electricity distribution companies in Ontario are required to act as the billing agent for all industry participants and must remit billed amounts accruing to these participants irrespective of whether such amounts are ultimately collected. With the exception of the debt retirement charge, electricity distribution companies are exposed to losses for entire amounts billed to customers. Electricity distribution companies are not compensated for assuming this level of risk nor is there a clear and mechanistic regulatory means to recover losses for non-distribution charges.

Management has implemented credit and collection policies in accordance with the OEB regulation to mitigate the exposure of the Corporation to credit risk. Such policies have significantly improved credit loss experience with respect to residential customers. However, OEB regulation continues to impose certain restrictions on credit policy that exposes electricity distribution corporations to unmitigated and uncompensated credit risk of several multiples of their means to generate revenue.

Extraordinary event risk

Unforeseen extraordinary events could disrupt the ability of the electricity distribution business to deliver electricity to all or some of its customers. These risks include weather disasters, major accidents or other involuntary events that may affect the electricity distribution system.

The Corporation has no obligation to deliver an uninterrupted supply of electricity due to extraordinary events, thereby avoiding third party liability concerns.

The Corporation may make application to the Ministry of Energy for rate increases to recover costs incurred as a result of extraordinary circumstances impacting the electricity distribution system.

OUTLOOK

The reliable, efficient and safe delivery of electricity continues to be the primary focus of the Corporation through its regulated electricity distribution business. The Corporation operates the third largest municipally owned electricity distribution business in Ontario.

On October 17, 2006, the Ontario Government announced that publicly-owned utilities will be exempt for two years from paying electricity transfer tax when they sell electricity assets to other publicly-owned utilities in Ontario. The Corporation, with the experience and success of the Horizon Utilities' merger, and as one of the lowest cost, most efficient providers of electricity distribution in Ontario, is well positioned to bring further efficiencies to electricity distribution customers as the industry continues to rationalize and consolidate.

The Corporation is also committed to its multi-utility strategy to offer other utility services, such as water billing and customer care provided to the City of Hamilton and those services provided by FibreWired and Hamilton Community Energy, where internal skills and competencies support the delivery of such services in a manner that generates commercial returns on invested capital and creates value for its customers.



The Corporation remains committed to containing and reducing costs through process improvement and expanding its customer base across its existing and new utility businesses to achieve economies of scale and scope.

With the exception of certain non-recurring capital commitments described above, the capital program of the Corporation remains largely routine related to the replacement of existing infrastructure.

The Corporation has conservative levels of debt capitalization that strongly support its debt servicing obligations.

Overall, management believes that these strategies and conditions are favourable towards providing debt-holders with necessary assurances for current and ongoing investment in the Corporation.

**Hamilton Utilities Corporation
Auditors' Report to the Shareholder
and Consolidated Financial Statements
Years Ended December 31, 2006 and
December 31, 2005**



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AUDITORS' REPORT TO THE SHAREHOLDER

We have audited the consolidated balance sheets of Hamilton Utilities Corporation ("the Corporation") as at December 31, 2006 and 2005 and the consolidated statements of income and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these 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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2006 and 2005 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

A handwritten signature in black ink that reads 'KPMG LLP'. The signature is written in a cursive, slightly slanted style. Below the signature is a long, horizontal, slightly wavy line that underlines the text.

Chartered Accountants

Hamilton, Canada
February 2, 2007



Consolidated Balance Sheets

(in thousands)

As at December 31,

	2006	2005
ASSETS		
Current assets		
Cash and cash equivalents	\$ 33,306	\$ 46,613
Accounts receivable	81,759	86,345
Inventory	6,902	5,859
Other assets [note 4]	3,074	1,551
	125,041	140,368
Fixed assets [note 5]	297,437	286,864
Goodwill [note 3]	18,923	18,923
Future payments in lieu of taxes [note 6]	3,014	1,525
Deferred debt issuance costs	1,674	1,968
Total assets	\$ 446,089	\$ 449,648
LIABILITIES AND SHAREHOLDER'S EQUITY		
Current liabilities		
Accounts payable and accruals	\$ 72,849	\$ 92,951
Credit support for service delivery [note 7]	21,092	19,166
	93,941	112,117
Long-term liabilities		
Long-term borrowings [note 8]	105,000	105,000
Employee future benefits [note 9]	16,041	15,679
Net regulatory liabilities [note 10]	14,902	13,655
	135,943	134,334
Total liabilities	229,884	246,451
Minority interest [note 11]	34,996	33,205
Shareholder's equity		
Share capital [note 12]	129,897	129,897
Contributed surplus [note 3]	15,218	15,218
Retained earnings	36,094	24,877
Total shareholder's equity	181,209	169,992
Total liabilities and shareholder's equity	\$ 446,089	\$ 449,648

Commitments and contingencies [note 14]

On behalf of the Board:

Director

Director



Consolidated Statements of Income and Retained Earnings

(in thousands)

For the years ended December 31,

	2006	2005
Revenue		
Electricity distribution services charges <i>[note 15]</i>	\$ 79,610	\$ 76,815
Telecommunications services charges <i>[note 16]</i>	8,188	7,605
Electricity, heating and cooling services charges <i>[note 16]</i>	2,951	2,893
Total revenue	90,749	87,313
Other income from operations <i>[notes 16 and 17]</i>	9,299	7,339
	100,048	94,652
Expenses:		
Operating expenses <i>[note 19]</i>	44,491	46,037
Depreciation and amortization <i>[note 5]</i>	22,328	20,999
	66,819	67,036
Income from operating activities	33,229	27,616
Recovery of qualifying transition costs <i>[note 3]</i>	2,779	-
Gain on sale of fixed assets	129	610
Interest income	1,294	1,155
Interest expense <i>[note 8]</i>	(8,070)	(7,784)
Income before payments in lieu of taxes	29,361	21,597
Payments in lieu of income and large corporations taxes <i>[note 6]</i>	(9,971)	(6,920)
Net income before minority interest	19,390	14,677
Minority interest <i>[note 11]</i>	(3,148)	(2,308)
Net income	16,242	12,369
Retained earnings, beginning of year	24,877	35,660
Dividends paid	(5,016)	(23,088)
Refundable dividend tax on hand	(9)	(64)
Retained earnings, end of year	\$ 36,094	\$ 24,877

Consolidated Statements of Cash Flows

(in thousands)

For the years ended December 31,

	2006	2005
OPERATING ACTIVITIES		
Net income for the year	\$ 16,242	\$ 12,369
Add (deduct) non-cash items:		
Depreciation and amortization	23,286	21,963
Minority interest	3,148	2,308
Future payments in lieu of taxes	(1,489)	(2,715)
Net change in employee future benefits	362	184
Gain on sale of fixed assets	(129)	(610)
Net change in other assets and liabilities	(16,539)	27,289
Cash provided by operating activities	24,881	60,788
INVESTING ACTIVITIES		
Additions to fixed assets	(33,902)	(21,538)
Proceeds received on disposal of fixed assets	170	651
Cash used in investing activities	(33,732)	(20,887)
FINANCING ACTIVITIES		
Repayment of long-term borrowings	-	(29,123)
Dividends paid in the year	(5,016)	(23,088)
Net change in credit support for service delivery	1,926	338
Cash received on amalgamation	-	2,680
Minority interest dividend	(1,357)	(8,937)
Refundable dividend tax on hand	(9)	(64)
Cash used in financing activities	(4,456)	(58,194)
Net (decrease) in cash and cash equivalents during		
the year	(13,307)	(18,293)
Cash and cash equivalents, beginning of year	46,613	64,906
Cash and cash equivalents, end of year	\$ 33,306	\$ 46,613
Supplemental disclosure of cash flow information		
Interest received	\$ 1,294	\$ 1,092
Interest paid	\$ (6,821)	\$ (7,114)
Taxes paid	\$ (11,353)	\$ (12,891)



Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

1) BUSINESS OF CORPORATION

On June 1, 2000, Hamilton Utilities Corporation (the “Corporation”) was incorporated under the Business Corporations Act (Ontario). The Corporation is an investment holding company with investments in Horizon Utilities Corporation (“Horizon Utilities”), a regulated electricity distribution company, Horizon Holdings Inc. (“Horizon Holdings”), an investment holding company, and Hamilton Hydro Services Inc. (“HHSI”), a company operating telecommunications, district energy and retail services.

2) SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in Canada, consistently applied. The more significant accounting policies are summarized below:

a) Basis of consolidation

The consolidated financial statements include the accounts of the corporation and its subsidiaries, some of which have a minority interest. The principal operating companies and the Corporation’s ownership in these companies are as follows:

Horizon Holdings	78.9%
Horizon Utilities	78.9%
HHSI	100.0%

All significant inter-company accounts and transactions have been eliminated.

b) Regulation

The Ontario Energy Board Act, 1998 (Ontario) (“OEBA”) conferred on the Ontario Energy Board (“OEB”) increased powers and responsibilities to regulate the electricity industry in Ontario. These powers and responsibilities include approving or fixing rates for the transmission and distribution of electricity, providing continued rate protection for rural and remote electricity consumers, and ensuring that distribution companies fulfill obligations to connect and service customers. The OEB may also prescribe license requirements and conditions of service to electricity distributors which may include, among other things, record keeping, regulatory accounting principles, separation of accounts for distinct businesses, and filing and process requirements for rate setting purposes.

Rate Setting

The Company’s distribution rates are based on a revenue requirement that provides a regulated rate of return on the amount of shareholder’s equity supporting the business of electricity distribution. Distribution rates for 2005 were based on an annual rate of return of 9.88% on the amount of common equity deemed to be allocated to this business, presently regulated at 40% of the Corporation’s investment in electricity distribution assets and related working capital requirements.



Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

2) SIGNIFICANT ACCOUNTING POLICIES (Continued)

b) Regulation (continued)

As mandated by the OEB, the rate increase in 2005 was subject to a financial commitment by the Corporation to invest \$7,071 in conservation and demand management activities over the period September 1, 2005 to September 30, 2007.

Rate Setting (continued)

On April 12, 2006, the OEB approved the Corporation's Electricity Distribution Rate Application for 2006 distribution rates, for rates to be effective May 1, 2006. The 2006 distribution rate, in accordance with the OEB filing requirements, provides for a revised rate of return of 9.0%, as compared to 9.88% in previous years.

In accordance with the OEB Report on Cost of Capital and 2nd Generation Incentive Regulation for Ontario's Electricity Distributors, distribution rates for 2007 will be established based on an OEB approved incentive regulation mechanism model ("the IRM Model"). The IRM Model adjusts base rates for the 2006 Canada Gross Domestic Product Implicit Price Index less a Productivity Factor of 1% as determined by the OEB.

Regulatory Accounting

In its capacity to approve or set rates, the OEB has the authority to specify regulatory accounting treatments that may differ from Canadian generally accepted accounting principles for enterprises operating in a non-rate regulated environment. The OEB has the general power to include or exclude costs, revenues, losses or gains in the rates of a specific period, resulting in a change in the timing of accounting recognition from that which would have applied in an unregulated company. Such change in timing involves the application of rate regulated accounting, giving rise to the recognition of regulatory assets and liabilities. The Corporation's regulatory assets represent certain amounts receivable from future customers and costs that have been deferred for accounting purposes because it is probable that they will be recovered in future rates. The Corporation's regulatory liabilities represent costs with respect to non-distribution market related charges and variances in recoveries that are expected to be settled in future periods. Specific regulatory assets and liabilities are disclosed in Note 10.

The Electricity Restructuring Act (Ontario), 2004 (the "ERA")

On December 9, 2004, the Province enacted the ERA, which provides for a restructuring of Ontario's electricity sector to promote the expansion of electricity supply and capacity, alternative and renewable energy sources, and conservation and demand management. Under the ERA, the commodity cost of electricity for certain customer classes will be determined by the OEB on an annual basis and based on a combination of regulated, contract and competitive market prices for electricity. There are few provisions in the ERA that apply to electricity distributors.



Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

2) SIGNIFICANT ACCOUNTING POLICIES (Continued)

b) Regulation (continued)

Smart Meter Initiative

The Province of Ontario has committed to have “Smart Meter” electricity meters installed in 800,000 homes and small businesses by the end of 2007 and throughout Ontario by the end of 2010. Smart Meters permit consumption to be recorded within specific time intervals and specific tariffs to be levied within such intervals. *Bill 21, Energy Conservation and Responsibility Act*, provides the legislative framework and regulations to support this initiative.

In support of this initiative, the Corporation launched a Smart Meter pilot program in 2006 as part of its conservation and demand management plan approved by the OEB. The primary purpose of the pilot was to develop and test the processes, tools and network infrastructure to support mass deployment in 2007 to 2010.

Included in distribution rates effective May 1, 2006 is a charge for smart meters of \$0.39 per metered customer per month. Consistent with the OEB’s direction and pending further guidance, all smart meter related expenditures and recoveries are currently being deferred in regulatory accounts.

c) Measurement uncertainty

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and note disclosures related thereto. Due to the inherent uncertainty in making estimates, actual results could differ from estimates recorded in preparing these financial statements, including changes as a result of future regulatory decisions.

Accounts receivable and regulatory assets are stated after evaluation of amounts expected to be collected and an appropriate allowance for doubtful accounts. Inventory is recorded net of provisions for obsolescence. Amounts recorded for depreciation and amortization of equipment are based on estimates of useful service life.

d) Cash and cash equivalents

Cash equivalents comprise overnight deposits in an investment account with a Schedule A bank. Investments are carried at cost, which approximates fair value.

e) Inventory

Inventory consists principally of construction and maintenance materials. Inventory is stated at the lower of cost and replacement value, with cost determined on an average cost basis.



Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

2) SIGNIFICANT ACCOUNTING POLICIES (Continued)

f) Fixed assets and depreciation

Fixed assets are recorded at cost, including the cost of work in process, and are removed from the accounts at the end of their estimated services lives, except in those instances where specific identification allows their removal at retirement or disposition. For specifically identifiable assets, gains or losses at retirement or on disposition are credited or charged to other income, otherwise, no gain or loss is recognized unless a sale has occurred.

Depreciation is calculated on a straight-line basis over the estimated service life of fixed assets as follows:

Land rights	50 years
Buildings	15-30 years
Electricity distribution infrastructure	25-30 years
Fibre cable and duct infrastructure	15-25 years
Heating and electricity generation infrastructure	25 years
Other fixed assets	3-15 years

Work in process reflects the cost of construction materials and applied labour and overheads consumed in partially completed capital projects and is not depreciated.

g) Deferred debt issuance costs

Deferred debt issuance costs comprise costs related to issuing long-term borrowings. Such costs are amortized into income on an effective yield basis in relation to the underlying long-term borrowings.

h) Goodwill

Goodwill represents the amount by which the purchase price of an acquired business exceeds the fair value of the net identifiable assets purchased.

Goodwill is not amortized and is evaluated for impairment on an annual basis, or more frequently if circumstances require, with any write-down of the carrying value of goodwill being charged against the results of operations. Goodwill impairment is assessed based on a comparison of the fair value of the reporting unit to the underlying carrying value of the reporting unit's net assets, including goodwill.



Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

2) SIGNIFICANT ACCOUNTING POLICIES (Continued)

i) Credit support for service delivery

Credit support for service delivery represents cash deposits from electricity distribution customers and retailers, as well as construction deposits.

Deposits from electricity distribution customers are applied against any unpaid portion of individual customer accounts. Customer deposits in excess of unpaid account balances are refundable to individual customers upon termination of their electricity distribution service. Customer deposits are also refundable to residential electricity distribution customers demonstrating an acceptable level of credit risk, as determined by the Corporation.

Pursuant to the Ontario Energy Board retail settlement code, the Corporation is entitled to security from retailers to guarantee the payment of the difference between the market price for electricity and the retailer's average contract price.

Construction deposits represent cash prepayments for the estimated cost of capital projects recoverable from customers and developers. Upon completion of the capital project these deposits are transferred to capital contributions in aid of construction.

j) Employee future benefits

The Corporation pays certain health, dental and life insurance benefits, under unfunded defined benefit plans, on behalf of its retired employees.

Employee future benefits are recorded on an accrual basis. The accrued benefit obligations and current service cost are calculated using the projected benefit method pro rated on service and reflect management's best estimate of certain underlying assumptions. The current service cost for a period is equal to the actuarial present value of benefits attributed to that period in which employees rendered their services. Past service costs from plan amendments are amortized on a straight-line basis over the average remaining service period of employees active at the date of the amendment. The excess of actuarial gains (losses) over 10% of the accrued benefit obligation are amortized into expense on a straight-line basis over the expected average remaining service life of active employees.

k) Pension plan

The Corporation provides a pension plan for its employees through the Ontario Municipal Employees Retirement System ("OMERS"). OMERS is a multi-employer pension plan which operates as the Ontario Municipal Employees Retirement Fund ("the Fund"), and provides pensions for employees of Ontario municipalities, local boards, public utilities and school boards. The fund is a contributory defined benefit pension plan. The Corporation records the required contributions as an expense in the period they accrue.

l) Related party transactions

Transactions with related parties represent the culmination of the earnings process and are measured at the exchange amount.



Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

2) SIGNIFICANT ACCOUNTING POLICIES (Continued)

m) Payments in Lieu of Taxes (“PILs”)

The Corporation is currently exempt from taxes under the Income Tax Act (Canada) (“ITA”) and the Ontario Corporations Tax Act (“OCTA”).

Commencing October 1, 2001 and pursuant to the *Energy Competition Act* (“ECA”), the Corporation is required to compute taxes under the ITA and OCTA and remit such amounts thereunder to the Ontario Electricity Financial Corporation (“OEFC”). These amounts, referred to as PILs under the ECA, are applied to reduce certain debt obligations of the former Ontario Hydro continuing in OEFC.

The Corporation provides for PILs using the asset and liability method. Under this method, future tax assets and liabilities are recognized, to the extent such are determined likely to be realized, for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the date of enactment or substantive enactment.

PILs recoverable from loss carry-forwards are recorded in other assets at future statutory tax rates reflecting when such loss carry-forwards are expected to be utilized.

n) Capital contributions in aid of construction

Capital contributions arise from development charges which are provided and paid by developers and used to finance additions to fixed assets. Capital contributions received are treated as a “credit” contra account and are included in fixed assets. These amounts are subsequently amortized by a charge to accumulated amortization and a credit to amortization expense at an equivalent rate to that used for the depreciation of the related fixed asset.

o) Revenue recognition

Electricity distribution services charges

These charges comprise charges to customers for use of the Corporation’s electricity distribution system. These charges are recorded when the related services are performed.

Telecommunications services charges

These charges are recorded when the related services are performed. Installation revenue associated with the provisioning of the service is recognized over the term of the contract.



Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

2) SIGNIFICANT ACCOUNTING POLICIES (Continued)

Electricity, heating and cooling services charges

These charges comprise customer billings for the supply and distribution of electricity and thermal energy. Customer billings for these charges are recorded on the basis of a fixed monthly capacity charge, as well as customer usage.

3) HORIZON UTILITIES CORPORATION

On March 1, 2005, the former Hamilton Hydro Inc. (“HHI”), a regulated electricity distribution company then wholly-owned by the Corporation, merged with St. Catharines Hydro Utility Services Inc. (“SCHUSI”), also a regulated distribution company then wholly-owned by St. Catharines Hydro Inc. (“SCHI”), by amalgamation under the *Business Corporations Act (Ontario)* and continue as Horizon Utilities Corporation.

The amalgamation was completed pursuant to a Merger Co-operation Agreement dated November 25, 2004 between the City of Hamilton, as sole shareholder of the Corporation, and The Corporation of The City of St. Catharines, as sole shareholder of SCHI, which acknowledged their approval of the merger of HHI and SCHUSI under terms and conditions set out in a Merger Participation Agreement (the “MPA”), dated November 25, 2004, between the Corporation, HHI, SCHI and SCHUSI.

The MPA provided that the respective shareholders of HHI and SCHUSI, the Corporation and SCHI, receive common shares in Horizon Utilities with votes and value in proportion to the respective values of HHI and SCHUSI.

A valuation of HHI and SCHUSI was undertaken by a competent third party and was largely based on projections of capital assets, capital expenditures and operating expenses anticipated to be permitted by regulation administered by the OEB in its approval of allowable distribution charges for each respective corporation. The values agreed to by the Corporation and SCHI (the “Parties”) were as negotiated by the Parties based on such valuation. The results of the negotiation and valuation provide for common share allocations of 78.9% for the Corporation and 21.1% for SCHI.

In accordance with the MPA, immediately prior to the merger, HHI declared a dividend in specie to the Corporation consisting of the right to receive any future amounts received by Horizon Utilities that represent the recovery of any regulatory assets in excess of HHI’s book value of such assets as at February 28, 2005. SCHUSI also declared a dividend in specie to SCHI consisting of the right to receive any future amounts received by Horizon Utilities that represent the recovery of any regulatory assets in excess of SCHUSI’s book value of such assets as at February 28, 2005. In April 2006, the OEB approved Horizon Utilities’ application for the recovery of regulatory asset balances as at December 31, 2004, resulting in amounts recoverable by the Corporation and SCHI under the MPA of \$2,779 and \$2,935 respectively.

On March 1, 2005 Horizon Utilities issued the following shares in exchange for all of the issued and outstanding shares of HHI and SCHUSI:

	<u>No. Shares</u>
Class 1 Common owned by the Corporation	7,890
Class A Common owned by SCHI	2,110

Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

3) HORIZON UTILITIES CORPORATION (Continued)

This transaction resulted in the Corporation receiving a controlling interest in Horizon Utilities. The transaction was recorded by Horizon Utilities using the purchase method of accounting. As such, the results of operations and cash flow for 2005 reflect that of Horizon Utilities for the ten months ended December 31, 2005 and HHI for the two months ended February 28, 2005.

The purchase consideration was determined by the fair value of the assets and liabilities assumed as at March 1, 2005 and adjusted for the costs related to the merger, including direct costs associated with the transaction as well as human resource and other integration costs.

The total purchase consideration was allocated to identifiable net assets acquired based on their respective fair values as at the date of amalgamation as follows:

Purchase consideration comprised of:	
Issuance of 2,110 Class A common shares at fair value	55,052
Transaction and integration costs	3,545
Total purchase consideration	58,597
Fair value of net assets of SCHUSI acquired:	
Current assets	27,449
Fixed assets	56,498
Other assets	2,068
Current liabilities	(14,151)
Long-term liabilities	(32,190)
Net assets acquired	39,674
Excess purchase consideration over fair value of net assets acquired, allocated to goodwill	18,923

The excess of the fair value of the Class A common shares issued to SCHI over the stated capital of SCHUSI immediately prior to the merger has been recorded as contributed surplus on the balance sheet, and that, subsequent to amalgamation, a dividend was paid to SCHI in the amount of \$8,931 of which \$7,374 was charged to contributed surplus.

In addition to transaction and integration costs included as part of the total purchase consideration, the Corporation also incurred \$2,689 in additional costs related to the amalgamation, which have been included in operating expenses. These additional costs included severance costs associated with voluntary retirement and separation programs offered to employees, computer programming and other administrative costs related to the integration of operations.

The merger of HHI and SCHUSI results in the third largest municipally owned electricity distribution company in the Province serving approximately 230,000 customers in the municipalities of Hamilton and St. Catharines.

Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

4) OTHER ASSETS

Other assets comprise:

	2006	2005
Prepaid expenses	1,568	1,483
Current PILs receivable	1,438	-
Other	68	68
Total other assets	3,074	1,551

5) FIXED ASSETS

Fixed assets comprise:

	2006			2005		
	Original Cost	Accumulated Depreciation	Net Book Value	Original Cost	Accumulated Depreciation	Net Book Value
Land	1,493	-	1,493	1,493	-	1,493
Land rights	129	(42)	87	129	(39)	90
Buildings	26,713	(14,016)	12,697	25,350	(12,919)	12,431
Electricity distribution infrastructure	421,673	(175,607)	246,066	400,296	(161,901)	238,395
Fibre cable and duct infrastructure	18,182	(7,985)	10,197	16,845	(6,986)	9,859
Heating and electricity generation infrastructure	10,104	(1,442)	8,662	10,096	(1,038)	9,058
Other fixed assets	43,797	(29,874)	13,923	39,151	(27,536)	11,615
Work in process	4,312	-	4,312	3,923	-	3,923
	526,403	(228,966)	297,437	497,283	(210,419)	286,864

During the year, the Corporation received \$3,603 (2005 - \$2,453) of capital contributions in aid of construction.

Total depreciation expense for the year is \$23,286 (2005 - \$21,963) of which \$958 (2005 - \$964) has been allocated to operating expenses and capital.

6) PAYMENTS IN LIEU OF TAXES

The provision for PILs varies from amounts which would be computed by applying the Corporation's combined statutory income tax rate as follows:

	2006	2005
Basic rate applied to income before PILs	36.12%	36.12%
Increase (decrease) in PILs resulting from:		
Tax basis of depreciable capital assets and goodwill in excess of accounting basis	(2.88%)	(4.74%)
Revaluation of Future Tax Liability at 2011 statutory rate of 32.50%	1.14%	-
Items not deductible for tax purposes and other	(0.32%)	(0.24%)
Provision for payments in lieu of large corporations taxes	(0.10%)	0.90%
Effective rate applied to income before PILs	33.96%	32.04%

Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

6) PAYMENTS IN LIEU OF TAXES (Continued)

At year-end, based on substantively enacted income tax rates, future income tax assets of \$17,511 (2005 - \$20,379) have not been recorded. Such future income tax assets relate to tax bases of depreciable capital assets and employee future benefits in excess of amounts recorded for accounting purposes. Such future tax assets have not been recorded in the accounts as there is uncertainty as to whether the Corporation will realize the benefits related to these assets which would be realized as relatively modest reductions of future tax liability over many future years.

7) CREDIT SUPPORT FOR SERVICE DELIVERY

Credit support for service delivery comprises:

	2006	2005
Customer deposits	14,256	12,698
Retailer deposits	551	766
Construction deposits	6,285	5,702
Total credit support for service delivery	21,092	19,166

8) LONG-TERM BORROWINGS

Long-term borrowings comprise:

	2006	2005
Senior unsecured debentures bearing interest at 6.25% and due July 31, 2012	105,000	105,000

During the year, the Corporation accrued and paid interest in respect of the senior unsecured debentures in the amount of \$6,563 (2005 - \$6,563).

9) EMPLOYEE FUTURE BENEFITS

The Corporation pays certain health, dental and life insurance benefits on behalf of its retired employees. The Corporation accrues the cost of these employee future benefits over the periods in which the employees earn the benefits. The cost of employee future benefits earned by employees is actuarially determined applying the projected benefit method pro rated on length of service. Significant assumptions underlying the valuation include management's best estimate of the interest (discount) rate, salary escalation, the average retirement age of employees, employee turnover and expected health and dental care costs.

Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

9) EMPLOYEE FUTURE BENEFITS (Continued)

Information about the Corporation's defined benefit plan is as follows:

	2006	2005
Accrued benefit liability, beginning of year	15,679	12,427
Fair value of liability assumed on acquisition of SCHUSI	-	3,068
Net benefit expense:		
Current service cost	348	250
Interest cost	980	981
Amortization of net actuarial loss	94	(14)
Net benefit expense for the year	1,422	1,217
Benefits paid for the year	(1,060)	(1,033)
Accrued benefit liability, end of year	16,041	15,679

An actuarial valuation of the plan obligations was completed as at December 31, 2003, and March 1, 2005 for Horizon Utilities, resulting in an unamortized net actuarial loss of \$1,067. The Corporation has adopted the corridor method of accounting for the actuarially determined experience gains (losses). The excess of actuarial gains (losses) over 10% of the accrued benefit obligation is amortized into expense on a straight-line basis over the expected average remaining service life of active employees.

The main actuarial assumptions underlying the valuation are as follows:

a) General inflation

The health care cost trend for prescription drugs is estimated to increase at a declining rate from 7% to 4% over five years. Other medical and dental expenses are assumed to increase at 4% per year.

The approximate effect on the accrued benefit obligation and the estimated net benefit expense if the health care trend rate assumption was increased or decreased by 1% is as follows:

	Accrued Benefit Obligation	Periodic Benefit Cost
1% increase in health care trend rate	2,241	110
1% decrease in health care trend rate	(1,781)	(89)

b) Interest (discount) rate

The obligations at year-end, the present value of future liabilities, and the expense for the period ended, were determined using a discount rate of 5.0% representing an estimate of the yield on high quality corporate bonds as at the valuation date.

m) Salary levels

Future general salary and wage levels were assumed to increase at 4% per year.

Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

10) NET REGULATORY ASSETS (LIABILITIES)

Net regulatory assets (liabilities) comprise:

	2006	2005
Settlement variances	(8,880)	(23,571)
Regulatory assets recovery account	(2,560)	-
Other	(2,850)	2,714
Smart Meter deferral account	(612)	-
Pre-market opening cost of power variances	-	7,202
Total net regulatory liabilities	(14,902)	(13,655)

Net regulatory assets (liabilities) represent costs incurred by the Corporation and settlement variances with other participants in the electricity market, less recoveries, for the purpose of supporting the deregulation of the electricity industry in Ontario. These amounts have been accumulated pursuant to regulation underlying the EA and deferred in anticipation of their future recovery in electricity distribution service charges.

Settlement variances - represent amounts that have accumulated since January 1, 2005 and have not yet been approved in rates by the OEB and comprise:

- i) variances between amounts charged by the Independent Electricity System Operator (“IESO”) for the operation of the wholesale electricity market and grid, various wholesale market settlement charges and transmission charges, and the amounts billed to customers by the Corporation based on the OEB approved wholesale market service rate; and,
- ii) variances between the amounts charged by the IESO to allow for purchases of imported electricity and the amounts billed to customers by the Corporation based on OEB approved rates.

Regulatory asset recovery account – represents approved regulatory asset balances as at December 31, 2004, consisting of transition costs, pre-market opening cost of power variances, settlement variances and associated interest, less amounts recovered up to December 31, 2006. Recoveries in excess of approved amounts will be repaid to customers over a two-year period ending April 30, 2008.

Pre-market opening cost of power variances - represent the excess of the cost of the commodity electricity to the Corporation over the amount billed to its customers prior to Market Opening. This variance was subsequently approved and included in the regulatory asset recovery account.

Smart Meter deferral account – represents the deferral of operating expenditures, capital expenditures and revenues related to Smart Meters in accordance with the direction set out by the OEB.

In the absence of rate regulated accounting, generally accepted accounting principles would require the Corporation to reverse the carrying charges recorded, related to the regulatory assets (liabilities) described above, in the operating results for the year in which they are incurred. In 2006, carrying charges of \$360 were recorded in interest expense (2005 – nil).

Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

11) MINORITY INTEREST

Minority interest represents SCHI's 21.1% common share ownership in Horizon Utilities and Horizon Holdings and comprises:

	2006	2005
Minority interest, beginning of year	33,205	-
Minority interest on acquisition of SCHUSI [note 3]	-	39,834
Net income for the period	3,148	2,308
Dividends paid to minority interest	(1,357)	(8,937)
Minority interest, end of year	34,996	33,205

12) SHARE CAPITAL

The authorized share capital consists of an unlimited number of common shares. Any invitation to the public to subscribe for shares of the Corporation is prohibited. On July 1, 2002, the Corporation issued 1,000 voting common shares for consideration of \$129,897.

13) PENSION PLAN

The Corporation participates in the Ontario Municipal Employees Retirement Fund (OMERS), a multi-employer plan, on behalf of its employees. The plan is a contributory defined benefit pension plan. Contributions during the year were 6.5% for employee earnings below the year's maximum pensionable earnings and 9.6% thereafter. Contributions are expected to remain the same in 2007. During 2006, the Corporation expensed contributions totaling \$1,908 (2005 - \$1,601) made to OMERS in respect of the employer's required contributions to the plan.

14) COMMITMENTS AND CONTINGENCIES

Commitments

Credit Facility

Pursuant to a Second Amended and Restated Credit Agreement ("Credit Facility") dated January 20, 2006 with a Canadian chartered bank, the Corporation can borrow up to \$100,000 to finance general corporate requirements, working capital requirements and prudential obligations. Borrowings may be in the form of Bankers' Acceptances ("BAs"), prime rate loans, letters of credit, and/or current account overdrafts. The Amended Credit Facility matures on January 19, 2009. Interest rates payable on the Amended Credit Facility are based on a margin above prime or the BA rate, as the case may be, determined by reference to the Corporation's debt rating. A standby fee is paid on any unutilized portion of the Amended Credit Facility.

No amounts were drawn under the facility at year-end (2005 – nil).

The Corporation has issued a \$23,500 letter of credit in favour of the Independent Electricity System Operator ("IESO") as security for Horizon Utilities purchase of electricity through the IESO. At year-end, no amounts were drawn on the letters of credit.



Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

14) COMMITMENTS AND CONTINGENCIES (Continued)

Commitments (continued)

Contractual Obligations

Pursuant to a Meter Supply and Services Agreement executed on January 30, 2007, the Corporation has committed to purchase Smart Meters and related equipment over a one-year period. The total commitment over the term of the contract is approximately \$5,500.

Pursuant to the terms of a Master Purchase/Sale Agreement dated April 1, 2003, the Corporation has agreed to purchase a fixed quantity of natural gas at a fixed price over five years. The total commitment over the term of the agreement is \$4,460 and the remaining commitment at year-end is \$1,233 (2005 - \$2,146). This commitment is part of a risk management strategy to provide the Corporation with sufficient quantities of natural gas at a fixed price to meet the requirements to produce, sell and distribute electrical energy pursuant to an agreement with the City of Hamilton (*note 13*).

Pursuant to the terms of a Maintenance Contract dated August 25, 2003, the Corporation has agreed to purchase engine maintenance services for a period of 15 years or 60,000 engine hours, whichever comes first. The total commitment over the term of the agreement is approximately \$1,941 and the remaining commitment at year-end is approximately \$1,600. Included in the contract price is the cost of a major engine overhaul of approximately \$300.

Leases

The Corporation has entered into operating leases for office space and computer equipment. Minimum annual lease payments required are as follows:

2007	436
2008	448
2009	448
2010	249
Thereafter	1,529
Total	3,110

Contingencies

A class action claiming \$500,000 in restitutionary payments plus interest was served on the former Toronto Hydro-Electric Commission, continuing as Toronto Hydro Corporation, on November 18, 1998. The action was initiated against the former Toronto Hydro-Electric Commission as the representative of the Defendant Class consisting of all municipal electric utilities (“MEU”) in Ontario, of which the Corporation is a successor MEU, which have charged Late Payment charges on overdue utility bills at any time after April 1, 1981.



Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

14) COMMITMENTS AND CONTINGENCIES (Continued)

Contingencies (continued)

The claim is that late payment penalties result in municipal electric utilities receiving interest at effective rates in excess of 60% per year, which is illegal under Section 347(1)(b) of the Criminal Code. This action is at a preliminary stage. Pleadings have closed but examinations for discovery have not been conducted and the classes have not been certified. The Electricity Distributors Association is undertaking the defense of this class action on behalf of the Defendant Class.

On April 22, 2004, in a decision in a class action commenced against The Consumers' Gas Company Limited (now Enbridge Gas Distribution Inc.), the Supreme Court of Canada ruled that Consumers' Gas was required to repay that portion of certain late payment charges collected by it from its customers that were in excess of the interest limit stipulated in section 347 of the Criminal Code. Although the claim related to charges collected by Consumers' Gas after the enactment of section 347 of the Criminal Code in 1981, the Supreme Court limited recovery to charges collected after the action was initiated in 1994. The Supreme Court remitted the matter back to the Ontario Superior Court of Justice for determination of the damages. The parties have reached a tentative settlement of this class action but the settlement is subject to approval by the Ontario Superior Court of Justice. The Court held a hearing in September 2006 to consider the settlement but has not yet issued a ruling.

The Corporation is not a party to the Consumers' Gas class action, however, it is anticipated that the above noted class action will now proceed for determination in light of the reasons of the Supreme Court in the Consumers' Gas class action.

The Defendant Class may have defences available to it in this action that were not disposed of by the Supreme Court in the Consumers' Gas class action. Also, the determination of whether the late payment charges collected by the Corporation from its customers were in excess of the interest limit stipulated in section 347 of the Criminal Code is fact specific in each circumstance.

At this time, given the preliminary status of this action, it is not possible to quantify the effect, if any, on the financial statements of the Corporation. Consequently, no provision has been made in these financial statements with respect to any possible losses that may arise as a result of this matter.

15) BILLINGS TO ELECTRICITY DISTRIBUTION CUSTOMERS

The Corporation, through its subsidiary, Horizon Utilities, is licensed by the OEB to distribute electricity. As a licensed distributor, the Corporation is responsible for billing customers for electricity generated by third parties and the related costs of providing electricity service, such as transmission and other services, provided by third parties. The Corporation is required, pursuant to regulation, to remit such amounts to these third parties, irrespective of whether the Corporation ultimately collects these amounts from customers. The Corporation may file to recover uncollected debt retirement charges from OEFC once each year. Otherwise, the Corporation is unable to recover uncollected amounts formerly remitted to these third parties. The Corporation retains only its electricity distribution services charge that is regulated by the OEB.

Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

15) BILLINGS TO ELECTRICITY DISTRIBUTION CUSTOMERS (Continued)

Electricity distribution services charges comprise:

	2006	2005
Gross customer billings	515,881	548,951
Less: Pass through charges billed by the Corporation		
Electricity charges paid through to generators	(301,908)	(333,823)
Transmission and miscellaneous charges	(62,302)	(66,786)
Market service charges	(34,608)	(34,710)
Debt retirement charges	(37,453)	(36,817)
Total electricity distribution service charges	79,610	76,815

16) RELATED PARTY TRANSACTIONS

The Corporation provides certain water and wastewater billing and customer care services to its sole shareholder, the City of Hamilton. Other income includes \$2,901 (2005 - \$2,790) earned with respect to this agreement. As at the end of the year, accounts payable and accruals include \$8,839 (2005 - \$8,540) owing to the City of Hamilton for amounts collected on behalf of the City of Hamilton pursuant to this agreement.

Pursuant to agreements dated December 31, 2002, the Corporation produces, sells and distributes thermal and electrical energy to the City of Hamilton. Revenue earned during the year under the agreements was \$2,090 (2005 - \$2,073). The agreements expire December 31, 2027. The Corporation also earned \$1,093 (2005 - \$883) in telecommunications services revenue from the City of Hamilton.

As at the end of the year, accounts receivable includes \$1,416 (2005 - \$619) owing from the City of Hamilton.

17) OTHER INCOME FROM OPERATIONS

Other income from operations comprises:

	2006	2005
Water and wastewater billing and customer care charges	2,901	2,790
Collection and other service charges	2,296	1,192
Pole rental income	1,187	775
Water heater and sentinel light rental income	1,133	1,066
Late payment interest charges	873	937
Scrap sales	628	249
Miscellaneous	281	330
Total other income from operations	9,299	7,339



Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

18) FINANCIAL INSTRUMENTS

The carrying values of cash and cash equivalents, accounts receivable, credit support for service delivery, and accounts payable and accruals approximate fair values because of the short maturity of these instruments.

The 6.25% debentures due July 31, 2012, having a carrying value of \$105,000 (2005 – \$105,000)[*note 8*], have a fair value of \$114,188 (2005 - \$115,805) based on year-end quoted market prices for similar debt.

Financial assets held by the Corporation, such as accounts receivable, expose it to credit risk.

The Corporation earns its revenue from a broad base of customers located in the City of Hamilton and the City of St. Catharines. Two customers account for 6% and 1% of total revenue (2005 – 6% and 1%), one of which is the City of Hamilton, and the other a local school board. No other single customer in either year would account for revenue in excess of 1%.

One customer, the City of Hamilton, accounts for 3.7% of accounts receivable at year-end. No other single customer accounts for more than 1% of accounts receivable at year-end.

19) SEGMENTED INFORMATION

The Corporation has four reportable business segments: electricity distribution operations under the business name of Horizon Utilities, telecommunications and related operations under the business name of FibreWired, district energy operations under the business name of Hamilton Community Energy (HCE) and all other, which includes corporate activities and the elimination of inter-segment transactions.

Each segment represents a strategic business unit of the Corporation offering distinct products and services and requiring different technology and marketing strategies.

Inter-segment sales and transfers are accounted for as if the sales and transfers were to third parties.

Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

19) SEGMENTED INFORMATION (Continued)

The following table presents the results of the Corporation from continuing operations by reportable segment for 2006:

	Horizon				Total
	Utilities	FibreWired	HCE	Other	
Revenue	79,610	8,188	2,951	-	90,749
Other income	9,837	12	-	(550)	9,299
	89,447	8,200	2,951	(550)	100,048
Operating expenses	37,953	4,969	2,390	(821)	44,491
Depreciation	19,945	1,720	510	153	22,328
Recovery of qualifying transition costs	-	-	-	(2,779)	(2,779)
Gain on sale of assets	(50)	(70)	-	(9)	(129)
Interest income	(792)	(14)	-	(488)	(1,294)
Interest expense	9,229	261	-	(1,420)	8,070
PILs	8,197	349	(25)	1,450	9,971
Expenses, finance charges and PILs	74,482	7,215	2,875	(3,914)	80,658
Net income before minority interest	14,965	985	76	3,364	19,390
Minority interest	(3,158)	-	-	10	(3,148)
Net income	11,807	985	76	3,374	16,242
Total assets	404,597	13,706	12,425	15,361	446,089
Capital acquisitions	31,426	2,156	14	306	33,902

Notes to the Consolidated Financial Statements

December 31, 2006

(\$ in thousands)

19) SEGMENTED INFORMATION (Continued)

The following table presents the results of the Corporation from continuing operations by reportable segment for 2005:

	Horizon				
	Utilities	FibreWired	HCE	Other	Total
Revenue	76,815	7,605	2,893	-	87,313
Other income	7,650	2	-	(313)	7,339
	84,465	7,607	2,893	(313)	94,652
Operating expenses	39,508	4,333	2,739	(543)	46,037
Depreciation	18,599	1,775	496	129	20,999
Gain on sale of assets	(104)	(499)	-	(7)	(610)
Interest income	(931)	-	-	(224)	(1,155)
Interest expense	8,936	226	760	(2,138)	7,784
PILs	5,917	493	(399)	909	6,920
Expenses, finance charges and PILs	71,925	6,328	3,596	(1,874)	79,975
Net income (loss)					
before minority interest	12,540	1,279	(703)	1,561	14,677
Minority interest	(2,308)	-	-	-	(2,308)
Net income	10,232	1,279	(703)	1,561	12,369
Total assets	411,559	11,485	12,178	14,426	449,648
Capital acquisitions	18,848	1,482	968	240	21,538

20) COMPARATIVE FIGURES

Certain comparative data have been reclassified to conform with the presentation of the current year.