

1 Q. Please provide a copy of Hydro's Annual Financial Reports to the PUB from
2 2004 onwards.

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5 A. Please find attached a copy of Hydro's Annual Financial Returns to the PUB
6 for 2004 and 2005.

IC 51 NLH□
2006 General Rate Application□
Attachment 1

NEWFOUNDLAND AND LABRADOR HYDRO 2004 ANNUAL RETURN

**BOARD OF COMMISSIONERS
OF PUBLIC UTILITIES**
(filed pursuant to ss.59(2) of the
Public Utilities Act)



IN THE MATTER OF the *Public Utilities Act*, (the "Act"); and

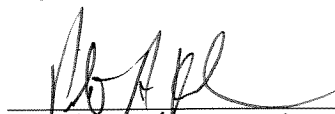
AND IN THE MATTER OF an Annual Return for 2004 filed by Newfoundland and Labrador Hydro pursuant to Section 59(2) of the Act

AFFIDAVIT

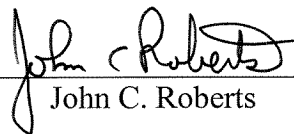
I, John C. Roberts, Chartered Accountant, of St. John's, in the Province of Newfoundland and Labrador, make oath and swear as follows:

1. THAT I am the Vice-President Finance and Chief Financial Officer for Newfoundland and Labrador Hydro, and as such I either have personal knowledge, or I have been so informed and do verily believe, as the case may be, of the matters and things contained in the within Newfoundland and Labrador Hydro 2004 Annual Return.
2. THAT I have read the contents of the within Annual Return and they are correct and true to the best of my knowledge, information and belief.

SWORN TO BEFORE ME in
the City of St. John's, in the Province
of Newfoundland and Labrador this 31st
day of March 2005.



Notary Public - Newfoundland and Labrador



John C. Roberts

NEWFOUNDLAND AND LABRADOR HYDRO
NON-CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2004



Deloitte & Touche LLP
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Canada

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Auditors' Report

To the Directors of
Newfoundland and Labrador Hydro

We have audited the balance sheet of Newfoundland and Labrador Hydro as at December 31, 2004 and the statements of income and retained earnings and cash flows for the year then ended. These financial statements have been prepared on a non-consolidated basis for regulatory purposes. The financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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 financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2004 and the results of its operations and its cash flows for the year then ended in accordance with the basis of accounting described in Note 1 to the financial statements. As required by The Hydro Corporation Act, we report that, in our opinion, these principles have been applied on a basis consistent with that of the preceding year.

These financial statements, which have not been, and were not intended to be, prepared in accordance with Canadian generally accepted accounting principles, are solely for the information and use of the Directors of Newfoundland and Labrador Hydro and the Board of Commissioners of the Public Utilities. The financial statements are not intended to be and should not be used by anyone other than the specified users or for any other purpose.

A handwritten signature in black ink, appearing to read "Deloitte & Touche LLP", written in a cursive, stylized script.

Chartered Accountants
February 15, 2005

BOARD OF DIRECTORS

DEAN MacDONALD
Chief Executive Officer
Persona Inc.

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Deputy Minister
Department of Natural Resources

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Retired

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Instrumar Ltd.

WILLIAM KELLY
Electrician
Wabush Mines

CRAIG TUCKER
Vice-President
M5 Marketing Communications Inc.

DR. DAVID SMALLWOOD
Educational Consultant

KEN MARSHALL
Vice President and General Manager
Rogers Cable - Atlantic Region

WILLIAM E. WELLS
President and Chief Executive Officer
Newfoundland and Labrador Hydro

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Vice-President, Human Resources, General Counsel and
Corporate Secretary

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Vice-President, Finance and Chief Financial Officer

FRED H. MARTIN
Vice-President, Transmission and Rural Operations

PETER A. HICKMAN
Assistant Corporate Secretary

MARK G. S. BRADBURY
Director, Finance

HEAD AND CORPORATE OFFICE

P.O. Box 12400
St. John's, Newfoundland and Labrador
A1B 4K7

NEWFOUNDLAND AND LABRADOR HYDRO
NON-CONSOLIDATED BALANCE SHEET

As at December 31 (millions of dollars)

	2004	2003
ASSETS		
Capital assets (Note 3)		
Capital assets in service	1,922.4	1,904.6
Less contributions in aid of construction	<u>85.1</u>	<u>85.1</u>
	1,837.3	1,819.5
Less accumulated depreciation	<u>481.8</u>	<u>456.7</u>
	1,355.5	1,362.8
Construction in progress	<u>52.2</u>	<u>46.5</u>
	1,407.7	1,409.3
Current assets		
Accounts receivable	56.0	44.6
Current portion of long-term receivable (Note 4)	40.1	32.2
Current portion of rate stabilization plan	8.6	-
Due from related party (Note 12)	0.2	-
Fuel and supplies at average cost	39.9	40.7
Prepaid expenses	<u>1.6</u>	<u>2.1</u>
	146.4	119.6
Sinking funds (Note 9)	87.1	70.1
Long-term receivable (Note 4)	93.9	123.5
Investments (Note 5)	312.1	299.7
Deferred charges (Note 6)	<u>84.7</u>	<u>88.7</u>
	<u>2,131.9</u>	<u>2,110.9</u>

See accompanying notes

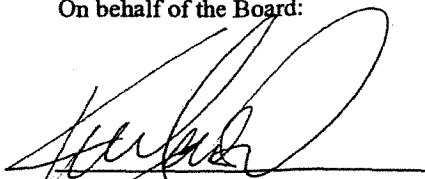
NEWFOUNDLAND AND LABRADOR HYDRO
NON-CONSOLIDATED BALANCE SHEET

As at December 31 (millions of dollars)

	2004	2003
LIABILITIES AND SHAREHOLDER'S EQUITY		
Long-term debt (Note 7)	1,355.5	1,363.8
Current liabilities		
Bank indebtedness	7.4	5.7
Accounts payable and accrued liabilities	40.8	42.4
Accrued interest	30.1	30.2
Long-term debt due within one year (Note 7)	13.8	13.4
Promissory notes (Note 7)	158.3	150.2
Due to related parties (Note 12)	-	4.1
	250.4	246.0
Rate stabilization plan	5.5	-
Employee future benefits (Note 8)	29.7	26.9
Shareholder's equity		
Share capital		
Common shares of par value of \$1 each		
Authorized 25,000,000 shares; issued 22,503,942 shares	22.5	22.5
Contributed capital		
Lower Churchill Development (Note 5)	15.4	15.4
Muskrat Falls Project	2.2	2.2
Retained earnings	450.7	434.1
	490.8	474.2
Commitments and contingencies (Note 11)		
	<u>2,131.9</u>	<u>2,110.9</u>

See accompanying notes

On behalf of the Board:


 DIRECTOR


 DIRECTOR

NEWFOUNDLAND AND LABRADOR HYDRO
NON-CONSOLIDATED STATEMENT OF INCOME AND RETAINED EARNINGS

<i>Year ended December 31 (millions of dollars)</i>	2004	2003
Revenue		
Energy sales	390.8	358.4
Recovery of costs in rate stabilization plan	34.2	16.7
Other	<u>2.2</u>	<u>2.2</u>
	<u>427.2</u>	<u>377.3</u>
Expenses		
Operations and administration (Note 12)	91.8	92.9
Fuels	83.1	84.6
Amortization of costs in rate stabilization plan	34.2	16.7
Power purchased (Note 12)	40.2	30.2
Depreciation	33.8	33.1
Interest (Note 10)	<u>96.5</u>	<u>92.1</u>
	<u>379.6</u>	<u>349.6</u>
Income from operations	<u>47.6</u>	<u>27.7</u>
Other revenue (expense)		
Equity in net income of CF(L)Co. (Note 5)	15.0	11.3
Preferred dividends from CF(L)Co.	6.9	7.2
Interest on share purchase debt (Note 10)	<u>(2.3)</u>	<u>(2.2)</u>
	<u>19.6</u>	<u>16.3</u>
Net income before unusual items	67.2	44.0
Unusual items		
Write-down of construction in progress (Note 3)	-	(9.6)
Write-down of investment in LCDC (Note 5 (b))	<u>-</u>	<u>(12.7)</u>
Net income	67.2	21.7
Retained earnings, beginning of year	<u>434.1</u>	<u>453.5</u>
	501.3	475.2
Dividends	<u>50.6</u>	<u>41.1</u>
Retained earnings, end of year	<u><u>450.7</u></u>	<u><u>434.1</u></u>

See accompanying notes

NEWFOUNDLAND AND LABRADOR HYDRO
NON-CONSOLIDATED STATEMENT OF CASH FLOWS

<i>Year ended December 31 (millions of dollars)</i>	2004	2003
Cash provided by (used in)		
Operating activities		
Net income	67.2	21.7
Adjusted for items not involving a cash flow		
Depreciation	33.8	33.1
Amortization of deferred charges	3.5	4.0
Equity in net income of CF(L)Co.	(15.0)	(11.3)
Rate stabilization plan	(3.1)	20.5
Loss on disposal of capital assets	1.8	3.2
Other	-	(0.6)
Write-down of construction in progress	-	9.6
Write-down of investment in LCDC	-	12.7
	88.2	92.9
Change in non-cash balances related to operations		
Accounts receivable	(11.4)	1.9
Fuel and supplies	0.8	(0.7)
Prepaid expenses	0.5	0.1
Long-term receivable	21.7	(51.4)
Accounts payable and accrued liabilities	0.5	(9.7)
Accrued interest	(0.1)	3.0
Due to related parties	(4.3)	0.2
Employee future benefits	2.8	1.9
	98.7	38.2
Dividends from CF(L)Co.	2.6	2.0
	101.3	40.2
Financing activities		
Long-term debt issued	-	125.0
Long-term debt retired	(3.4)	(7.4)
Increase (decrease) in promissory notes	8.1	(31.7)
Dividends	(50.6)	(41.1)
	(45.9)	44.8
Investing activities		
Net additions to capital assets	(35.0)	(64.6)
Proceeds on disposal of capital assets	1.0	0.8
Reductions (additions) to deferred charges	0.5	(3.9)
Increase in sinking funds	(21.5)	(19.2)
Change in accounts payable related to investing activities	(2.1)	0.3
	(57.1)	(86.6)
Net decrease in cash	(1.7)	(1.6)
Cash position, beginning of year	(5.7)	(4.1)
Cash position, end of year	(7.4)	(5.7)
Cash position is represented by		
Bank indebtedness	(7.4)	(5.7)
	(7.4)	(5.7)
Supplementary disclosure of cash flow information		
Interest income received	-	0.3
Interest paid	107.0	103.3

See accompanying notes

NEWFOUNDLAND AND LABRADOR HYDRO

NOTES TO NON-CONSOLIDATED FINANCIAL STATEMENTS

Newfoundland and Labrador Hydro ("Hydro") is incorporated under a special act of the Legislature of the Province of Newfoundland and Labrador ("Province") as a Crown corporation and is exempt from paying income taxes under Section 149 (1)(d) of the Income Tax Act. The principal activity of Hydro is the development, generation and sale of electric power.

1. PRINCIPLES OF FINANCIAL STATEMENT PRESENTATION

These financial statements have been prepared in accordance with the significant accounting policies set out below. These financial statements materially differ from Canadian generally accepted accounting principles because they are non-consolidated. Hydro's investments in its subsidiary and jointly controlled companies have been accounted for using the equity method of accounting. Consolidated financial statements for the same period have been prepared for presentation to the Lieutenant-Governor in Council of the Province.

Preparation of these financial statements requires the use of estimates and assumptions that affect the amounts reported and disclosed in these statements and related notes. Actual results may differ from these estimates.

2. SIGNIFICANT ACCOUNTING POLICIES

Rates and Regulations

Hydro's earnings from its electrical sales to most customers within the Province are regulated on the basis of return on rate base. As well, Hydro's borrowing and capital expenditure programs are subject to review and approval by the Public Utilities Board ("PUB").

Rates charged to rural customers do not recover the full costs of providing the service but Hydro recovers the resulting deficit from other customers.

Hydro has adopted selected accounting treatments that differ from that for enterprises not subject to rate regulation. The more significant of these include the following:

Rate Stabilization Plan

On January 1, 1986, Hydro, having received the concurrence of the PUB, implemented a rate stabilization plan ("RSP") which primarily provides for the deferral of cost variances resulting from changes in fuel prices, levels of precipitation and load. Adjustments are required in retail rates to cover the amortization of the balance in the plan and are implemented on July 1 of each year. Similar adjustments required in industrial rates are implemented on January 1 of each year.

RSP balances which accumulated prior to December 31, 2003 (Note 3), have been converted to a long-term receivable. Any subsequent balances accumulating in the RSP including financing charges, are to be recovered in the following year, with the exception of hydraulic variation, which will be recovered or refunded at a rate of twenty-five percent of the outstanding balance at year-end. Additionally, a fuel rider is calculated annually based on the forecast fuel price and is added or subtracted from the rates that would otherwise be in effect.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Rates and Regulations (cont'd.)

Foreign Exchange Losses

Foreign exchange losses related to long-term debt, including current portion, are subject to the rate setting process. The PUB has accepted the inclusion by Hydro of realized foreign exchange losses in rates charged to customers. Any such loss, net of any gain, not recovered due to the operation of the rate setting process is deferred to the time of the next rate hearing for inclusion in the new rates to be set at that time. This amortization is included in interest expense. Commencing in 2002, the PUB ordered Hydro's deferred foreign exchange losses, net of the \$10.0 million provision previously accumulated, be amortized over a forty-year period (Note 6).

Capital Assets and Depreciation

Hydro follows the capitalization and depreciation policies as described in Note 1, which have been approved by the PUB.

Deferred Regulatory Costs

In 2004, the PUB approved the deferral of external costs associated with the general rate application and hearing, in the amount of \$1,800,000, which is to be amortized over a 3 year period.

Cash Equivalents and Short-Term Investments

Cash equivalents and short-term investments consist primarily of Canadian treasury bills and banker's acceptances. Those with original maturities at date of purchase of three months or less are classified as cash equivalents whereas those with original maturities beyond three months and less than twelve months are classified as short-term investments. Both are stated at cost, which approximates market value. As at December 31, 2004 and 2003 there were no cash equivalents or short-term investments outstanding.

Capital Assets and Depreciation

Expenditures for additions, improvements and renewals are capitalized and normal expenditures for maintenance and repairs are charged to operations.

Construction in progress includes the costs incurred in preliminary feasibility studies, engineering and construction of new generation, transmission and distribution facilities. Interest is charged to construction in progress at rates equivalent to the weighted average cost of capital.

During 2004, Hydro adopted the recommendations of the Canadian Institute of Chartered Accountants' (CICA) Handbook Section 3110, *Asset Retirement Obligations*. This new accounting standard requires that the company recognize the fair value of the future expenditures required to settle legal obligations associated with the retirement of capital assets, to the extent that it is reasonably estimable. As it is expected that Hydro's assets will be used for an indefinite period, no removal date can be determined and consequently, a reasonable estimate of the fair value of any related asset retirement obligation cannot be determined at this time. If it becomes possible to estimate the fair value of the cost of removing assets that Hydro is legally required to remove, an asset retirement obligation will be recognized at that time.

Contributions in aid of construction are funds received from customers and governments toward the cost of capital assets. Contributions are treated as a reduction to capital assets and the net capital assets are depreciated.

Depreciation is calculated on hydroelectric generating plant and on transmission plant in service on the sinking fund method using interest factors ranging from 5.25% to 15.79%. Depreciation on other plant in service is calculated on the straight-line method. These methods are designed to fully amortize the cost of the facilities, after deducting contributions in aid of construction, over their estimated service lives.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Capital Assets and Depreciation (cont'd.)

Estimated service lives of the major assets are as follows:

Generation Plant	
Hydroelectric	50, 75 and 100 years
Thermal	25 and 30 years
Diesel	20 years
Transmission	
Lines	40 and 50 years
Switching stations	40 years
Distribution system	30 years
Other	3 to 50 years

Debt Discount and Financing Expenses

These costs are amortized on a straight-line basis over the lives of the respective debt issues.

Promissory Notes

Promissory Notes bear interest from 2.10% to 2.86% per annum (2003 - 2.66% to 2.93%) with carrying value approximating fair value due to their short-term nature.

Revenue Recognition

Revenue is recorded on the basis of power and energy deliveries made.

Foreign Currency Translation

Foreign currency transactions are translated into their Canadian dollar equivalent as follows:

- (a) At the transaction date, each asset, liability, revenue or expense is translated using exchange rates in effect at that date.
- (b) At each balance sheet date monetary assets and liabilities are adjusted to reflect exchange rates in effect at that date.

Financial Instruments

From time to time, Hydro enters into interest rate swap agreements to manage interest rate risk. Net receipts or payments under the swap agreements are recorded as adjustments to interest expense.

Employee Future Benefits

Employees participate in the Province's Public Service Pension Plan, a multiemployer defined benefit plan. The employer's contributions are expensed as incurred.

Hydro provides group life insurance and health care benefits on a cost-shared basis to retired employees, in addition to a severance payment upon retirement. The expected cost of providing these other employee future benefits is accounted for on an accrual basis, and has been actuarially determined using the projected benefit method prorated on service and management's best estimate of salary escalation, retirement ages of employees, and expected health care costs. The excess of cumulative net actuarial gains and losses over 10% of the accrued benefit obligation are amortized over the expected average remaining service life of the employee group, which is approximately twelve years.

3. CAPITAL ASSETS

	Capital Assets in Service	Contributions In aid of Construction	Accumulated Depreciation	Construction In Progress
<i>millions of dollars</i>	2004			
Generation Plant				
Hydroelectric	829.6	20.5	39.6	0.2
Thermal	228.1	-	177.4	-
Diesel	56.9	6.5	24.1	0.4
Transmission and Distribution	628.9	55.1	136.2	0.2
Other	<u>178.9</u>	<u>3.0</u>	<u>104.5</u>	<u>51.4</u>
	<u>1,922.4</u>	<u>85.1</u>	<u>481.8</u>	<u>52.2</u>
	Capital Assets in Service	Contributions In aid of Construction	Accumulated Depreciation	Construction In Progress
<i>millions of dollars</i>	2003			
Generation Plant				
Hydroelectric	826.5	20.5	36.0	0.2
Thermal	227.0	-	175.7	-
Diesel	59.5	6.7	23.4	-
Transmission and Distribution	616.2	54.9	123.1	0.6
Other	<u>175.4</u>	<u>3.0</u>	<u>98.5</u>	<u>45.7</u>
	<u>1,904.6</u>	<u>85.1</u>	<u>456.7</u>	<u>46.5</u>

As at December 31, 2003 Management reviewed the carrying balance of its Construction in Progress related to the Labrador Hydro Project. As Hydro had been unable to successfully conclude development plans at that time, it decided to write-down the balance by \$9.6 million to its best estimate of net recoverable amount.

4. LONG-TERM RECEIVABLE

<i>millions of dollars</i>	2004	2003
Rate Stabilization Plan		
Retail	101.7	114.8
Industrial	<u>32.3</u>	<u>40.9</u>
	134.0	155.7
Less current portion of long-term receivable	<u>40.1</u>	<u>32.2</u>
	<u>93.9</u>	<u>123.5</u>

This receivable bears interest at the weighted average cost of capital which is approximately 7.2% and is to be recovered over a five-year period, which commenced in 2003.

5. INVESTMENTS

<i>millions of dollars</i>	Ownership Interest	2004	2003
Churchill Falls (Labrador) Corporation Limited	65.8%		
Shares, at cost		167.2	167.2
Equity in retained earnings at beginning of year		129.8	120.5
Equity in net income for the year		15.0	11.3
Dividends for the year		(2.6)	(2.0)
		309.4	297.0 (a)
Lower Churchill Development Corporation Limited	51.0%	2.7	2.7 (b)
Gull Island Power Company Limited	100.0%	-	- (c)
		<u>312.1</u>	<u>299.7</u>

- (a) The cost of the investment in Churchill Falls (Labrador) Corporation Limited ("CF(L)Co.") exceeded the equity in the book value of the net assets acquired by \$77.1 million. This amount is assigned to capital assets and is being amortized on a straight-line basis at the rate of 1.5% per annum. As at December 31, 2004, \$34.7 million (2003 \$33.6 million) had been amortized.

A portion of Hydro's shareholding in CF(L)Co. is deposited in a voting trust pursuant to an agreement with Hydro-Québec.

Effective June 18, 1999, the two shareholders of CF(L)Co., Hydro and Hydro-Québec, entered into a shareholders' agreement which provided, among other matters, that certain of the strategic operating, financing and investing policies of CF(L)Co. be subject to approval jointly by representatives of Hydro and Hydro-Québec. CF(L)Co. also receives certain benefits from Hydro-Québec, including significant revenues from Hydro-Québec under a guaranteed winter availability contract through 2041.

- (b) The Lower Churchill Development Corporation Limited ("LCDC") was established with the objective of developing all or part of the hydroelectric potential of the Lower Churchill River ("Lower Churchill Development") in Labrador.

Hydro, the designate for the Province's shareholding in LCDC, holds 1,540 Class A common shares of LCDC. 520 shares were acquired in 1979 pursuant to the signing of an Option Agreement between LCDC and the Province, dated November 24, 1978, and expiring November 24, 2005. 510 shares were acquired in each of the years 1980 and 1981, by way of capital contributions from the Province.

As at December 31, 2003, Management reviewed the carrying balance of its Capital Studies related to the development of the Lower Churchill Basin. As LCDC had been unable to successfully conclude development plans at that time, it decided to write-down the balance of \$25.0 million. Hydro's investment in LCDC was reduced by \$12.7 million which represents its proportionate share of the write-down.

- (c) Gull Island Power Company Limited ("GIPCo.") is incorporated under the laws of Canada. Its objective was to develop the hydroelectric potential at Gull Island on the Lower Churchill River in Labrador, and construct a direct current transmission system from Labrador to the island of Newfoundland ("Gull Island Project"). All project costs were funded by way of capital contributions from the Province. Hydro suspended all work on the Gull Island Project in 1976, in the absence of satisfactory arrangements for the financing of the project and the marketing of available power.

Upon agreement to continue with the Lower Churchill Development, the GIPCo. assets will be sold to LCDC pursuant to the provisions of the Option Agreement.

As at December 31, 2003, Management reviewed the carrying balance of the Gull Island Project. As GIPCo. had been unable to successfully conclude development plans at that time, it decided to write-down that balance by \$96.3 million. This write-down was not reflected in the non-consolidated statements as the shareholding was carried at \$100.

6. DEFERRED CHARGES

<i>millions of dollars</i>	2004	2003
Debt discount, financing expenses and other	11.9	15.1
Accumulated amortization	<u>7.0</u>	<u>8.4</u>
	<u>4.9</u>	<u>6.7</u>
Foreign exchange losses realized	96.3	96.3
Accumulated provision	<u>10.0</u>	<u>10.0</u>
	<u>86.3</u>	<u>86.3</u>
Accumulated amortization	<u>6.5</u>	<u>4.3</u>
	<u>79.8</u>	<u>82.0</u>
Net deferred charges	<u>84.7</u>	<u>88.7</u>

7. LONG-TERM DEBT

Series	Interest Rate %	Year of Issue	Year of Maturity	2004	2003
<i>millions of dollars</i>				2004	2003
AC	5.05	2001	2006	200.0	200.0
AA	5.50	1998	2008	200.0	200.0
V	10.50	1989	2014	125.0	125.0 (a)
X	10.25	1992	2017	150.0	150.0 (a)
Y	8.40	1996	2026	300.0	300.0 (a)
AB	6.65	2001	2031	300.0	300.0 (a)
AD	5.70	2003	2033	<u>125.0</u>	<u>125.0</u> (a)
Total debentures				1,400.0	1,400.0
Less sinking fund investments in own debentures				<u>48.3</u>	<u>43.8</u>
				1,351.7	1,356.2
Government of Canada loans at 5.25% to 7.91% maturing in 2006 to 2014				16.4	18.8
Other				<u>1.2</u>	<u>2.2</u>
				1,369.3	1,377.2
Less payments due within one year				<u>13.8</u>	<u>13.4</u>
				<u>1,355.5</u>	<u>1,363.8</u>

(a) Sinking funds have been established for these issues.

Promissory notes, debentures and long-term loans are unsecured and unconditionally guaranteed as to principal and interest and where applicable, sinking fund payments, by the Province. The Province charges Hydro a guarantee fee of one percent annually on the total debt (net of sinking funds) guaranteed by the Province, outstanding as of the preceding December 31.

Required repayments of long-term debt and sinking fund requirements over the next five years will be as follows:

<i>millions of dollars</i>	2005	2006	2007	2008	2009
	13.8	212.7	12.8	212.9	13.1

The payments due within one year include sinking fund requirements of \$10.0 million (2003 - \$10.0 million).

8. EMPLOYEE FUTURE BENEFITS

Pension Plan

Employees participate in the Province's Public Service Pension Plan, a multiemployer defined benefit plan. The employer's contributions of \$3.4 million (2003 - \$3.4 million) are expensed as incurred.

Other Benefits

Additionally, Hydro provides group life insurance and healthcare benefits on a cost-shared basis to retired employees, and in certain cases, their surviving spouses, in addition to a severance payment upon retirement. The most recent actuarial valuation was performed as at December 31, 2004.

<i>millions of dollars</i>	2004	2003
Accrued benefit obligation		
Balance at beginning of year	33.6	32.0
Current service cost	1.3	1.0
Interest cost	2.4	2.2
Actuarial loss	3.5	-
Benefits paid	(1.5)	(1.6)
Balance at end of year	<u>39.3</u>	<u>33.6</u>
Plan deficit	39.3	33.6
Unamortized actuarial loss	(9.3)	(6.3)
Unamortized past-service cost	(0.3)	(0.4)
Accrued benefit liability at end of year	<u>29.7</u>	<u>26.9</u>
<i>millions of dollars</i>	2004	2003
Current service cost	1.3	1.0
Interest cost	2.4	2.2
Actuarial losses	<u>3.5</u>	<u>-</u>
	7.2	3.2
Adjustments		
Difference between actual actuarial loss and amount recognized	<u>(2.9)</u>	<u>0.3</u>
Benefit expense	<u>4.3</u>	<u>3.5</u>

The significant actuarial assumptions used in measuring the company's accrued benefit obligations and benefit expense are as follows:

	2004	2003
Discount rate	6.3%	7.0%
Rate of compensation increase	3.5%	3.5%

Assumed healthcare trend rates:

	2004	2003
Initial healthcare expense trend rate	12.0%	12.0%
Cost trend decline to	5.0%	5.0%
Year that rate reaches the rate it is assumed to remain at	2010	2010

A 1% change in assumed healthcare trend rates would have had the following effects for 2004:

	Increase	Decrease
Current service cost	0.2	(0.2)
Interest cost	0.4	(0.3)
Accrued benefits obligation	5.8	(5.2)

9. FINANCIAL INSTRUMENTS

Fair Value

The estimated fair values of financial instruments as at December 31, 2004 and 2003 are based on relevant market prices and information available at the time. The fair value of long-term debt is estimated based on the quoted market price for the same or similar debt instruments. The fair value estimates below are not necessarily indicative of the amounts that Hydro might receive or incur in actual market transactions. As a significant number of Hydro's assets and liabilities, including fuels and supplies and capital assets, do not meet the definition of financial instruments, the fair value estimates below do not reflect the fair value of Hydro as a whole.

	Carrying Value	Fair Value	Carrying Value	Fair Value
<i>millions of dollars</i>	2004		2003	
Financial Assets				
Sinking funds	87.1	96.9	70.1	76.3
Financial Liabilities				
Long-term debt including amount due in one year	1,369.3	1,679.4	1,377.2	1,661.6

Cash and cash equivalents, short-term investments, accounts receivable, bank indebtedness, accounts payable, accrued interest, promissory notes and due to related parties, are all short-term in nature and as such their carrying value approximates fair value. At December 31, 2004 approximately 62.2% (2003 - 63.3%) of the total accounts receivable balance outstanding is due from a regulated utility.

Sinking Funds

Sinking fund investments consist of bonds, debentures, promissory notes and coupons issued by, or guaranteed by, the Government of Canada or any province of Canada, and have maturity dates ranging from 2009 to 2033. Hydro debentures which Management intends to hold to maturity are deducted from long-term debt while all other sinking fund investments are shown separately on the balance sheet as assets. Annual contributions to the various sinking funds are as per bond indenture terms, and are structured to ensure the availability of adequate funds at the time of expected bond redemption. Effective yields range from 4.77% to 9.86% (2003 - 5.33% to 9.86%).

10. INTEREST EXPENSE

<i>millions of dollars</i>	2004	2003
Gross interest		
Long-term debt	103.1	100.4
Promissory notes	4.1	5.7
	107.2	106.1
Amortization of debt discount and financing expenses	1.0	0.9
Amortization of foreign exchange losses	2.2	2.2
	110.4	109.2
Less		
Interest capitalized during construction	3.6	7.3
Interest earned	22.6	21.5
	84.2	80.4
Less		
Interest attributable to CF(L)Co. share purchase debt	2.3	2.2
Net interest attributable to Hydro	81.9	78.2
Debt guarantee fee	14.6	13.9
Net interest and guarantee fee	96.5	92.1

11. COMMITMENTS AND CONTINGENCIES

- (a) Hydro has received claims instituted by various companies and individuals with respect to outages and other miscellaneous matters. The aggregate of these claims, less any amounts that have been provided for in Hydro's financial statements is approximately \$7.7 million (2003 - \$15.0 million). The final resolution of these matters is currently under negotiation.

Legal proceedings have been commenced against Hydro by one of its customers claiming approximately \$22.2 million related to outages and plant shutdowns. Hydro is defending this claim and Management believes that this claim will not be successful.

- (b) Outstanding commitments for capital projects total approximately \$5.7 million at December 31, 2004 (2003 - \$12.8 million).

12. RELATED PARTY TRANSACTIONS

<i>millions of dollars</i>	2004	2003
Due to GIPCo. - promissory notes at 2.65% (2003 - 3.65%)	0.1	3.6
- other	-	0.1
Due to (from) CF(L)Co. - other	<u>(0.3)</u>	<u>0.4</u>
	<u>(0.2)</u>	<u>4.1</u>

- (a) Hydro has entered into a long-term power contract with CF(L)Co. for the purchase of \$6.2 million (2003 - \$6.3 million) of the power produced by CF(L)Co.
- (b) Under an agreement between Hydro and CF(L)Co., Hydro provides certain engineering, technical, management and administrative services to CF(L)Co. These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties. For the year ended December 31, 2004 the fees paid to Hydro for these services amounted to approximately \$2.1 million (2003 - \$1.8 million).

13. COMPARATIVE FIGURES

Certain of the 2003 comparative figures have been reclassified to conform with the 2004 financial statement presentation.

**NEWFOUNDLAND and LABRADOR HYDRO
BOARD OF DIRECTORS (as of December 31, 2004)**

<u>Name and Business Address</u>	<u>Residence</u>	<u>Officer</u>
WILLIAM E. WELLS President and Chief Executive Officer Newfoundland and Labrador Hydro P.O. Box 12400 St. John's, Newfoundland and Labrador A1B 4K7	17 Simms Street St. John's, Newfoundland and Labrador A1B 2A1	President and CEO
DEAN MacDONALD President and Chief Executive Officer Persona Communications Inc. 17 Duffy Place P.O. Box 12155, Station "A" St. John's, Newfoundland and Labrador A1B 4L1	4 Leeds Place St. John's, Newfoundland and Labrador A1A 5A4	Chairman
BARBARA FONG Executive Vice-President Instrumar Limited 3 rd Floor, Ultramar Building 39 Pippy Place P.O. Box 13246, Station A St. John's, Newfoundland and Labrador A1B 4A5	21 Church Hill #501 St. John's, Newfoundland and Labrador A1C 3Z8	No
WILLIAM KELLY Electrician Wabush Mines P.O. Box 3000 Wabush, Newfoundland and Labrador A0R 1B0	22 Guy Street P.O. Box 231 Wabush, Newfoundland and Labrador A0R 1B0	No
BRUCE SAUNDERS Deputy Minister Department of Natural Resources 7 th Floor, Natural Resources Building 50 Elizabeth Avenue St. John's, Newfoundland and Labrador A1A 1W5	31 Corcoran's Road Paradise, NL A1L 2A1	No
ELMER HARRIS Retired	9 Regina Place St. John's, Newfoundland and Labrador A1A 2R3	No

**NEWFOUNDLAND and LABRADOR HYDRO
BOARD OF DIRECTORS (as of December 31, 2004)**

<u>Name and Business Address</u>	<u>Residence</u>	<u>Officer</u>
DR. F. DAVID SMALLWOOD Retired	1 Marcelle Avenue Corner Brook, Newfoundland and Labrador A2H 2V6	No
KEN MARSHALL Vice-President and General Manager Rogers Cable - Atlantic Region 22 Austin Street St. John's, Newfoundland and Labrador A1B 3P2	14 Belfast Street St. John's, Newfoundland and Labrador A1B 2G6	No
CRAIG TUCKER Vice-President, Marketing M5 Marketing Communications Inc. P.O. Box 13305, Station "A" 42 O'Leary Avenue St. John's, Newfoundland and Labrador A1B 4B7	44 Duntara Crescent St. John's, Newfoundland and Labrador A1E 5Z1	No

**OFFICERS OF NEWFOUNDLAND and LABRADOR HYDRO
(AS OF DECEMBER 31, 2004)**

<u>Name and Business Address</u>	<u>Residence</u>
WILLIAM E. WELLS President and Chief Executive Officer (See list of Directors)	See list of Directors
DEAN MacDONALD Chairman (See list of Directors)	See list of Directors
JAMES R. HAYNES Vice-President Production Newfoundland and Labrador Hydro P.O. Box 12400 St. John's, Newfoundland and Labrador A1B 4K7	4 Mabledon Place St. John's, Newfoundland and Labrador A1A 3Y7
MAUREEN P. GREENE Vice-President Human Resources, General Counsel and Corporate Secretary Newfoundland and Labrador Hydro P.O. Box 12400 St. John's, Newfoundland and Labrador A1B 4K7	51 Mountbatten Drive St. John's, Newfoundland and Labrador A1A 3Y4
JOHN C. ROBERTS Vice-President, Finance and Chief Financial Officer Newfoundland and Labrador Hydro P.O. Box 12400 St. John's, Newfoundland and Labrador A1B 4K7	316 Stavanger Drive St. John's, Newfoundland and Labrador A1A 5X1
FRED MARTIN Vice-President, Transmission and Rural Operations Newfoundland and Labrador Hydro P.O. Box 12400 St. John's, Newfoundland and Labrador A1B 4K7	6 Eastmeadows Place St. John's, Newfoundland and Labrador A1A 3P3
PETER A. HICKMAN Assistant Corporate Secretary Newfoundland and Labrador Hydro P.O. Box 12400 St. John's, Newfoundland and Labrador A1B 4K7	12 Lunenburg Street St. John's, Newfoundland and Labrador A1A 5A3

**OFFICERS OF NEWFOUNDLAND and LABRADOR HYDRO
(AS OF DECEMBER 31, 2004)**

Name and Business Address

Residence

MARK G. S. BRADBURY

Director, Finance

Newfoundland and Labrador Hydro

P.O. Box 12400

St. John's, Newfoundland and Labrador

A1B 4K7

295 Frecker Drive

St. John's, Newfoundland and Labrador

A1E 5T8

Newfoundland and Labrador Hydro Computation of Rate Base (\$ 000s)		
Year Ended December 31		
	2004	2003
Capital Assets - Return 4	1,922,374	1,904,557
<u>Deduct:</u>		
Accumulated Depreciation - Return 6	481,801	456,695
Contributions in Aid of Construction - Return 7	85,081	85,055
Muskrat Falls Assets	2,149	2,049
Assets Not in Service	4	4
	<u>569,035</u>	<u>543,803</u>
Net Capital Assets	<u>1,353,339</u>	<u>1,360,754</u>
Net Capital Assets, Previous Year	<u>1,360,754</u>	<u>1,234,420</u>
Average Capital Assets	1,357,047	1,297,587
Cash Working Capital Allowance - Return 8	2,945	3,456
Fuel Inventory - Return 10	15,611	18,310
Supplies Inventory - Return 10	18,615	18,565
Average Deferred Foreign Exchange and PUB Costs - Return 11	<u>82,506</u>	<u>84,494</u>
Average Rate Base at Year-End - Return 12	<u><u>1,476,724</u></u>	<u><u>1,422,412</u></u>

Newfoundland and Labrador Hydro Plant Investment (\$ 000s)					
	Balance 1-Jan-04	Adjustments During 2004	Additions During 2004	Retirements During 2004	Balance 31-Dec-04
Power Generation					
Steam	181,571	-	2,650	(1,526)	182,695
Hydro	826,516	-	3,972	(861)	829,627
Diesel	59,468	-	62	(2,679)	56,851
Gas turbine	45,384	-	-	-	45,384
	1,112,939	-	6,684	(5,066)	1,114,557
Substations	172,446	(49)	2,045	(677)	173,765
Transmission	304,676	(447)	5,608	(286)	309,551
Distribution	139,115	491	6,982	(963)	145,625
General plant	91,052	31	3,060	(2,216)	91,927
Telecontrol	64,364	(25)	4,067	(2,812)	65,594
Computer software	13,845	-	1,276	-	15,121
Other	2,290	-	123	-	2,413
Total depreciable plant	1,900,727	1	29,845	(12,020)	1,918,553
Non depreciable land	3,830	-	-	(9)	3,821
Plant investment - Return 3	<u>1,904,557</u>	<u>1</u>	<u>29,845</u>	<u>(12,029)</u>	<u>1,922,374</u>
Work in progress					52,153
Total plant investment					<u><u>1,974,527</u></u>

Newfoundland and Labrador Hydro Capital Expenditures - Overview (\$ 000s)			
Year Ended December 31			
	Annual Budget 2004	Total Actual Expenditures 2004	Variance From 2004 Budget
Generation	4,049	3,759	(290)
Transmission and Rural Operations	11,999	14,298	2,299
General Properties	11,350	7,332	(4,018)
Allowance for Unforeseen Events	1,000	0	(1,000)
Projects Approved by PUB	2,798	2,389	(409)
New Projects Less than \$50,000 Approved by Hydro	239	206	(33)
Total Capital Budget	31,435	27,984	(3,451)
Approved P.U. 29 (2003)	27,316		
Approved P.U. 5 (2004)	1,534		
Approved P.U. 13 (2004)	303		
Approved P.U. 16 (2004)	465		
Approved P.U. 28 (2004)	258		
Approved P.U. 34 (2004)	95		
Carryover Projects 2003 to 2004	1,255		
New Projects Under \$50,000 approved by Hydro	209		
Total Approved Capital Budget	31,435		

Newfoundland and Labrador Hydro Accumulated Depreciation (\$ 000s)			
Balance, January 1, 2004			456,695
<u>Add:</u>			
Depreciation	33,801		
Adjustments	<u>0</u>		
			33,801
<u>Deduct:</u>			
Retirements			8,695
Balance, December 31, 2004 - Return 3			<u><u>481,801</u></u>
Depreciation Rates - 2004			
Steam - SL			5.56%
Hydro - SL			3.33%
Hydro - SF			6.93%
Gas Turbine - SL			4.00%
Diesel - SL			5.00%
Substations - SL			3.33%
Substations - SF			6.93%
Transmission - SL			3.33%
Transmission - SF			6.93%
Distribution - SL			3.33%
General Properties - SL	2.00%	-	33.33%
Telecontrol - SL	10.00%	or	20.00%
Software - SL			20.00%
Computer Hardware - SL	10.00%	or	33.33%
Percentage of accumulated depreciation to total depreciable plant			25.35%
Percentage of current depreciation to total depreciable plant			1.78%
Note: SL = straight-lined SF = sinking fund			

Newfoundland and Labrador Hydro
Contributions in Aid of Construction
 (\$ 000s)

	<u>CUSTOMERS</u>	<u>GOVERNMENT</u>	<u>TOTAL</u>
Gross Contributions January 1, 2004	13,288	71,767	85,055
2004 Retirements	(21)	(540)	(561)
2004 Additions	<u>587</u>	<u></u>	<u>587</u>
Balance December 31, 2004 - Return 3	<u><u>13,854</u></u>	<u><u>71,227</u></u>	<u><u>85,081</u></u>

Newfoundland and Labrador Hydro Working Capital (\$ 000s)		
Year Ended December 31		
	<u>2004</u>	<u>2003</u>
Calculation of Cash Working Capital Allowance		
Operating Expenses for the Year - Return 9	88,978	89,788
Deduct: Non Regulated Expenses	<u>250</u>	<u>(11)</u>
	88,728	89,799
Add: Power Purchases	<u>35,343</u>	<u>26,064</u>
Total	<u><u>124,071</u></u>	<u><u>115,863</u></u>
Working Capital Allowance (Total x 4.96% ; 2003 - 5.23%)	6,154	6,060
Deduct: HST Adjustment	<u>3,209</u>	<u>2,604</u>
Working Capital Allowance - Return 3	<u><u>2,945</u></u>	<u><u>3,456</u></u>
In general, the Company's billing and collection procedures are consistent with those in place during the preceding year.		

Newfoundland and Labrador Hydro Statement of Operating Costs (\$ 000s)		
Year Ended December 31		
	<u>2004</u>	<u>2003</u>
Net operating		
Salaries and fringe benefits	56,521	55,295
System equipment maintenance	17,416	18,212
Office supplies and expenses	1,858	1,984
Professional services	3,652	4,490
Insurance	1,682	1,655
Equipment rentals	1,274	1,458
Travel	2,243	2,256
Miscellaneous expenses	3,784	3,689
Building rental and maintenance	775	856
Transportation	1,808	1,914
Customer costs	811	677
Cost recoveries	<u>(2,846)</u>	<u>(2,698)</u>
Subtotal - Return 8	88,978	89,788
Loss on disposal of capital assets	<u>2,839</u>	<u>3,148</u>
Total operating costs	<u><u>91,817</u></u>	<u><u>92,936</u></u>

Newfoundland & Labrador Hydro
Significant Operating Expense Variances
(\$ 000s)

	<u>2004</u>	<u>2003</u>	<u>Increase (Decrease)</u>
Salaries and Fringe Benefits	56,521	55,295	1,226

Increased salaries and fringe benefits was primarily due to a general salary scale increase of 3.0% and an increase in employee future benefits expense arising from an updated actuarial valuation.

System Maintenance	17,416	18,212	(796)
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The decrease in this category of expenses was mainly due to lower maintenance costs at the Holyrood Thermal Plant (associated with a major overhaul of Unit #1 in 2003).

Professional Services	3,652	4,490	(838)
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The decrease in Professional Services category is mainly due to lower costs related to environmental services, software acquisition and regulatory hearings.

Loss on Disposal of Capital Assets	2,839	3,148	-
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The Loss on Disposal of Capital Assets was higher in 2003 due to items identified through records matching process as part of business process improvement efforts.

Newfoundland and Labrador Hydro Fuel and Supplies Inventory (\$ 000s)				
Year Ended December 31				
	Fuel		Supplies	
	2004	2003	2004	2003
Opening Balance	21,024	20,140	18,309	18,621
January	10,701	22,248	18,303	18,659
February	13,874	29,216	18,492	18,825
March	19,028	20,143	18,536	19,069
April	17,280	14,813	18,517	18,726
May	13,469	17,860	18,378	18,914
June	12,657	16,358	18,407	18,668
July	12,421	16,094	18,455	18,653
August	9,295	13,929	18,843	18,680
September	13,651	16,066	18,798	18,429
October	16,634	13,926	18,781	18,118
November	22,730	16,211	18,971	17,679
December	20,175	21,024	19,210	18,309
13 Month Average - Return 3	<u>15,611</u>	<u>18,310</u>	<u>18,615</u>	<u>18,565</u>

Newfoundland and Labrador Hydro Deferred Charges (\$ 000s)		
As at December 31		
	<u>2004</u>	<u>2003</u>
Unamortized debt discount, financing expenses and other	4,836	6,698
Foreign exchange losses realized	<u>79,807</u>	<u>81,964</u>
Total deferred charges, per financial statements	84,643	88,662
Deduct:		
Unamortized debt discount, financing expenses and other	4,836	6,698
Add:		
Unamortized PUB costs	<u>1,440</u>	<u>2,300</u>
Deferred Charges for Rate Base, end of current year	81,247	84,264
Deferred Charges for Rate Base, end of prior year	83,764 ¹	84,724
Average Deferred Charges for Rate Base - Return 3	<u><u>82,506</u></u>	<u><u>84,494</u></u>
1. The balance at the end of the prior year was adjusted by \$500,000 for 2004 average calculation to reflect the actual amount of PUB deferred costs approved in P.U. 14 (2004).		

Newfoundland and Labrador Hydro Return on Rate Base (\$ 000s)		
Year Ended December 31		
	2004	2003
(a) Corporate Net Income - Return 1	67,170	21,647
Deduct: Unregulated Earnings	59,849	24,235
Regulated Net Income (Loss)	7,321	(2,588)
Add: Interest - Return 16	96,527	92,138
(b) Regulated Earnings	<u>103,848</u>	<u>89,550</u>
(c) Average Rate Base - Return 3	<u>1,476,724</u>	<u>1,422,412</u>
(d) Rate of Return on Average Rate Base	<u>7.03%</u>	<u>6.30%</u>

Newfoundland and Labrador Hydro Return on Regulated Average Retained Earnings (\$ 000s)				
Year Ended December 31				
		<u>2004</u>		<u>2003</u>
Regulated Retained Earnings				
Ending Retained Earnings As Per Balance Sheet		450,628		434,049
Deduct: Non-Regulated Retained Earnings				
Beginning Non-Regulated Retained Earnings	229,122		239,699	
Non-Regulated Net Income for the year	59,849		24,235	
Non-Regulated Dividends for the year	<u>(49,355)</u>		<u>(34,812)</u>	
Ending Non-Regulated Retained Earnings		<u>239,616</u>		<u>229,122</u>
Regulated Retained Earnings, end of year		<u>211,012</u>		<u>204,927</u>
Regulated Retained Earnings, beginning of year		<u>204,927</u>		<u>213,789</u>
Regulated Average Retained Earnings		<u>207,970</u>		<u>209,358</u>
Earnings Applicable to Retained Earnings - Return 1		67,170		21,647
Deduct: Non-Regulated Net Income		<u>59,849</u>		<u>24,235</u>
Regulated Earnings (Loss)		<u>7,321</u>		<u>(2,588)</u>
Rate of Return on Regulated Average Retained Earnings		<u>3.52%</u>		<u>(1.24%)</u>

**Newfoundland and Labrador Hydro
Capital Structure
(\$ 000s)**

Year Ended December 31

Corporate

	2004		2003		Average	
	Amount	Percent	Amount	Percent	Amount	Percent
Debt (Note 1)	1,410,998	85.69%	1,433,093	86.33%	1,422,046	86.01%
Employee Future Benefits	29,715	1.80%	26,939	1.62%	28,327	1.71%
Retained Earnings - Hydro	205,933	12.51%	200,011	12.05%	202,972	12.28%
	1,646,646	100.00%	1,660,043	100.00%	1,653,345	100.00%

Regulated

	2004		2003		Average	
	Amount	Percent	Amount	Percent	Amount	Percent
Debt	1,357,457	84.94%	1,383,265	85.64%	1,370,361	85.29%
Employee Future Benefits	29,715	1.86%	26,939	1.67%	28,327	1.76%
Retained Earnings	211,012	13.20%	204,927	12.69%	207,970	12.94%
	1,598,184	100.00%	1,615,131	100.00%	1,606,658	100.00%

Note 1: Debt is the total debt per Return 15 with the Unamortized Debt Discount and Issue Expenses added back.

Newfoundland and Labrador Hydro			
Cost of Debt			
(\$ 000s)			
Year Ended December 31			
Corporate			
	<u>2004</u>	<u>2003</u>	<u>Average</u>
Long-Term Debt	1,369,266	1,377,170	1,373,218
Promissory Notes	158,285	150,236	154,261
Promissory Notes - Related Party	85	3,566	1,826
Sinking Funds	(87,124)	(70,098)	(78,611)
CF(L)Co Share Purchase Debt	(29,514)	(27,781)	(28,648)
Unamortized Debt Discount and Issue Expenses	<u>(3,396)</u>	<u>(4,398)</u>	<u>(3,897)</u>
Total Debt - Return 14	<u>1,407,602</u>	<u>1,428,695</u>	<u>1,418,149</u>
Interest Expense - 2004 Return 16			<u>110,660</u>
Cost of Debt			<u>7.80%</u>

Newfoundland and Labrador Hydro Interest Expense (\$ 000s)		
Year Ended December 31		
	<u>2004</u>	<u>2003</u>
Gross Interest		
Long-Term Debt	103,100	100,379
Promissory Notes	<u>4,131</u>	<u>5,727</u>
	107,231	106,106
Amortization of Debt Discount and Financing Expenses	996	896
Provision for Foreign Exchange	2,159	2,155
Interest Earned	(12,018)	(11,175)
Debt Guarantee Fee - Hydro	14,587	13,908
Deduct: Interest Attributable to CF(L)Co	<u>(2,295)</u>	<u>(2,165)</u>
Interest for Cost of Debt - Return 15	110,660	109,725
Deduct:		
Interest capitalized during construction	(3,595)	(7,254)
Interest earned on RSP	<u>(10,538)</u>	<u>(10,333)</u>
Net Interest Per Financial Statements - Return 1, 12	<u><u>96,527</u></u>	<u><u>92,138</u></u>

Newfoundland and Labrador Hydro Rate Stabilization Account - December 31, 2003 Plan (\$ 000s)					
Year Ended December 31					
Month	Utility		Industrial		Closing Balance
	Recovery	Interest	Recovery	Interest	
December 2003					155,704 ¹
January	(1,761)	663	(954)	236	153,888
February	(1,647)	657	(922)	232	152,208
March	(1,652)	651	(944)	228	150,491
April	(1,244)	645	(930)	224	149,186
May	(1,095)	642	(978)	220	147,975
June	(985)	639	(918)	216	146,927
July	(1,690)	673	(998)	223	145,135
August	(1,642)	666	(989)	219	143,389
September	(1,728)	660	(925)	214	141,610
October	(2,019)	654	(924)	210	139,531
November	(2,465)	646	(923)	205	136,994
December	(3,033)	635	(869)	201	133,928
	<u>(20,961)</u>	<u>7,831</u>	<u>(11,274)</u>	<u>2,628</u>	
1. The balance of both plans at December 31, 2003 were combined to one opening balance.					

Newfoundland and Labrador Hydro Rate Stabilization Account - January 2004 to December 2004 Plan (\$ 000s)										
Year Ended December 31										
Month	Utility					Cumulative Net Balance	Industrial			
	Load Variation	Allocation Fuel Variation	Allocation Rural Rate Alteration	Financing Charges	Adjustment		Load Variation	Allocation Fuel Variation	Financing Charges	Cumulative Net Balance
December 2003						-				-
January	(181,532)	1,539,843	(56,326)	-	-	1,301,985	34,666	403,540	-	438,206
February	(190,973)	1,667,884	(53,242)	7,522	-	2,733,176	128,948	444,950	2,532	1,014,636
March	(271,525)	1,562,157	(48,045)	15,790	-	3,991,553	(11,115)	423,670	5,862	1,433,053
April	(33,031)	1,234,053	(45,884)	23,059	-	5,169,750	21,202	390,837	8,279	1,853,371
May	(79,328)	556,083	(37,357)	29,866	-	5,639,014	113,400	191,843	10,707	2,169,321
June	(189,011)	319,017	(34,164)	32,577	-	5,767,433	48,795	90,410	12,532	2,321,058
July	(94,105)	3,052	(51,857)	35,172	(262,147)	5,397,548	201,056	5,203	14,155	2,541,472
August	(54,040)	179,320	(98,794)	32,916	(254,832)	5,202,118	177,953	57,530	15,499	2,792,454
September	(94,782)	323,342	(90,780)	31,724	(268,034)	5,103,588	198,569	98,640	17,029	3,106,692
October	89,990	711,444	(93,243)	31,123	(313,283)	5,529,619	249,843	191,524	18,946	3,567,005
November	165,179	1,151,566	(102,654)	33,721	(382,426)	6,395,005	53,752	311,757	21,753	3,954,267
December	238,431	553,938	(123,477)	38,999	(470,476)	6,632,420	68,056	165,888	24,114	4,212,325
Year to date	<u>(694,727)</u>	<u>9,801,699</u>	<u>(835,823)</u>	<u>312,469</u>	<u>(1,951,198)</u>	6,632,420	<u>1,285,125</u>	<u>2,775,792</u>	<u>151,408</u>	4,212,325
Hydraulic Allocation						<u>(1,722,445)</u>				<u>(487,788)</u>
Total						<u>4,909,975</u>				<u>3,724,537</u>
						To Return 18a				To Return 18a

Newfoundland and Labrador Hydro Rate Stabilization Account - January 2004 to December 2004 Plan (\$ 000s)						
Year Ended December 31						
Month	Hydraulic			From Return 18		Cumulative Net Balance
	Net Hydraulic Production Variation	Financing Charges	Cumulative Variation and Financing Charges	Utility Balance	Industrial Balance	
December 2003			-	-	-	-
January	(2,253,333)	-	(2,253,333)	1,301,985	438,206	(513,142)
February	(755,896)	(13,018)	(3,022,247)	2,733,176	1,014,636	725,565
March	(1,546,352)	(17,460)	(4,586,059)	3,991,553	1,433,053	838,547
April	1,822,393	(26,494)	(2,790,160)	5,169,750	1,853,371	4,232,961
May	(2,051,723)	(16,119)	(4,858,002)	5,639,014	2,169,321	2,950,333
June	(2,468,008)	(28,065)	(7,354,075)	5,767,433	2,321,058	734,416
July	(1,142,482)	(44,848)	(8,541,405)	5,397,548	2,541,472	(602,385)
August	1,935,464	(52,088)	(6,658,029)	5,202,118	2,792,454	1,336,543
September	186,538	(40,603)	(6,512,094)	5,103,588	3,106,692	1,698,186
October	(2,537,570)	(39,713)	(9,089,377)	5,529,619	3,567,005	7,247
November	741,403	(55,430)	(8,403,404)	6,395,005	3,954,267	1,945,868
December	707,529	(51,247)	(7,747,122)	6,632,420	4,212,325	3,097,623
Year to date	(7,362,037)	(385,085)	(7,747,122)			
Hydraulic Allocation	1,840,509	385,085	2,225,594	(1,722,445)	(487,788)	15,361
Total	<u>(5,521,528)</u>	<u>-</u>	<u>(5,521,528)</u>	<u>4,909,975</u>	<u>3,724,537</u>	<u>3,112,984</u>

Newfoundland and Labrador Hydro Assessable Revenue (\$ 000s)		
Year Ended December 31		
	2004	2003
Electricity Sales	390,758	358,396
Rate Stabilization	34,187	16,669
Other Revenue	2,240	2,256
	427,185	377,321
Deduct:		
Hydro Quebec Sales	44,142	32,604
Iron Ore Company of Canada	3,993	4,653
Insurance Refund of Loss on Rencontre East Fire	380	-
Error in Accrual of Rental Revenue From Aliant	(148)	148
Assessable Revenue	<u>378,818</u>	<u>339,916</u>

NEWFOUNDLAND & LABRADOR HYDRO
2004 Annual Report on the Rural Deficit

	2004 Actual			
	Revenues	Cost of Service Before Deficit and Revenue Allocation	Revenue Credits	Deficit
	(\$)	(\$)	(\$)	(\$)
Rural Deficit Areas				
Island Interconnected	33,181,005	48,784,479	(199,085)	(15,404,389)
Island Isolated	1,314,711	7,772,688		(6,457,977)
Labrador Isolated	4,898,441	20,689,894		(15,791,453)
L'Anse au Loup	1,431,966	3,302,812		(1,870,845)
DND Revenue Credit			(1,075,232)	1,075,232
Total	40,826,124	80,549,873	(1,274,317)	(38,449,432)

	2004 Actual ⁽¹⁾				
	Number of Communities ⁽²⁾	Number of Customers	Cost per kWh ⁽³⁾	Deficit per Customer ⁽³⁾	Cost Recovery Ratio ⁽³⁾
			(\$)	(\$)	
Rural Deficit Areas					
Island Interconnected	144	21,951	0.13	(702)	0.68
Island Isolated	8	943	0.85	(6,848)	0.17
Labrador Isolated	17	2,352	0.62	(6,714)	0.24
L'Anse au Loup	8	949	0.22	(1,971)	0.43
Total	177	26,195	0.19	(1,468)	0.51

	Forecast				
	Deficit 2005	Deficit 2006	Deficit 2007	Deficit 2008	Deficit ⁽⁴⁾ 2009
	(\$)	(\$)	(\$)	(\$)	(\$)
Rural Deficit Areas					
Island Interconnected	15,861,000	16,851,000	18,338,000	20,032,000	22,534,000
Isolated Systems	23,921,000	23,334,000	23,250,000	23,351,000	23,896,000
DND Revenue Credit	(1,253,000)	(1,843,000)	(2,448,000)	(3,147,000)	(3,104,000)
Total	38,529,000	38,342,000	39,140,000	40,236,000	43,326,000

⁽¹⁾ Average cost for Island Interconnected customers less Rural Interconnected is \$0.042 per kilowatthour and cost for Labrador Interconnected customers is \$0.017 per kilowatthour. Both calculations are based on kW.h sales.

⁽²⁾ Hydro's definition of Community corresponds to the "Town Code" in its customer information system. Some smaller communities may be combined if they share a single postal code.

⁽³⁾ Excludes DND Revenue Credit.

⁽⁴⁾ Operating and maintenance costs are projected to increase by inflation and no base rate increases have been assumed in the calculation the Island Interconnected Rural Deficit projection for the period 2005 to 2009. Approximately 40% of the projected increase is due to forecast higher No. 6 Fuel costs.

NEWFOUNDLAND & LABRADOR HYDRO
2004 Annual Report on the Rural Deficit

Specific initiatives that have been undertaken in 2004 to reduce the capital and operating costs for the rural systems include the following:

- In 2004, recommendations from the Reliability Centered Maintenance initiative were fully implemented. Resulting actions taken, such as reducing the frequency of overhauls on diesel engines, will assist in controlling the rural deficit in the longer term.
- Hydro applied for, and the Public Utilities Board approved, the interconnection of Recontre East. This was evaluated as the least cost alternative to provide long-term, reliable power to the community. The interconnection to the Provincial grid will be completed in 2005.
- Through its Hydrowise Energy Awareness Program, Hydro continues to inform its customers on ways to reduce energy consumption and save money. In 2004, Hydro distributed approximately 16,000 compact fluorescent lights to residential customers on its diesel systems. Through this initiative, energy usage on these systems should be reduced by about 1.2 GWh per year - the equivalent of 363,000 litres of fuel on an annual basis.
- Frontier Power Systems Inc. has commissioned all 6 turbines in the wind demonstration project in Ramea. During 2004, a total of approximately 110,000 kWhrs of energy was produced. In addition, discussions continue with Unity Bay Energy Limited on the potential establishment of a wind generation plant on the isolated system at St. Brendans. Should this proceed, Hydro would purchase the energy production on a "share the saving" principle up to a maximum of 90% of Hydro's avoided diesel fuel cost. The proponent is anticipating a capacity of approximately 100 kW.
- Hydro is supporting the Battle Harbour Assisted Living Corporation study the potential of utilizing waste heat from the Mary's Harbour Diesel Plant to augment oil fired energy sources at their personal home care facility in that community. Work included preliminary engineering and the preparation of cost estimates and schedules. Should the project proceed, Hydro would expect to recover 100% of its capital costs and share in any fuel savings. Hydro also advised the Corporation as to various agencies through which capital funding could be realized.

NEWFOUNDLAND AND LABRADOR HYDRO 2005 ANNUAL RETURN

**BOARD OF COMMISSIONERS
OF PUBLIC UTILITIES**
(filed pursuant to ss.59(2) of the
Public Utilities Act)




AND IN THE MATTER OF an Annual Return
for 2005 filed by Newfoundland and Labrador Hydro
pursuant to Section 59(2) of the Act

I, Derrick F. Sturge, Chartered Accountant, of St. John's, in the Province of Newfoundland and Labrador, make oath and swear as follows:

- SWORN TO BEFORE ME in
the City of St. John's, in the Province
of Newfoundland and Labrador this 17th
day of April 2006.**

Geo. M. J.
Barrister, Newfoundland
and Labrador

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)
)
)
)


Derrick F. Sturge

NEWFOUNDLAND AND LABRADOR HYDRO
NON-CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2005

Deloitte

Deloitte & Touche LLP
10 Factory Lane
Fort William Building
St. John's NL A1C 6H5
Canada

Tel: (709) 576-8480
Fax: (709) 576-8460
www.deloitte.ca

Auditors' Report

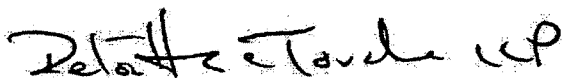
To the Directors of
Newfoundland and Labrador Hydro

We have audited the balance sheet of Newfoundland and Labrador Hydro as at December 31, 2005 and the statements of income and retained earnings and cash flows for the year then ended. These financial statements have been prepared on a non-consolidated basis for regulatory purposes. The financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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 financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2005 and the results of its operations and its cash flows for the year then ended in accordance with the basis of accounting described in Note 1 to the financial statements. As required by The Hydro Corporation Act, we report that, in our opinion, these principles have been applied on a basis consistent with that of the preceding year.

These financial statements, which have not been, and were not intended to be, prepared in accordance with Canadian generally accepted accounting principles, are solely for the information and use of the Directors of Newfoundland and Labrador Hydro and the Board of Commissioners of Public Utilities. The financial statements are not intended to be and should not be used by anyone other than the specified users or for any other purpose.



Chartered Accountants
February 14, 2006

BOARD OF DIRECTORS

DEAN T. MacDONALD
Chief Executive Officer
Persona Inc.

EDMUND J. MARTIN
President and Chief Executive Officer
Newfoundland and Labrador Hydro

TOM CLIFT
Associate Dean Academic Programs
Faculty of Business
Memorial University of Newfoundland

BRUCE SAUNDERS
Deputy Minister
Department of Natural Resources

EDNA TURPIN
Consultant

GERALD J. SHORTALL
Chartered Accountant

WILLIAM KELLY
Retired

LINDA SHEPPARD
Assistant Manager
Newfoundland and Labrador Credit Union

CRAIG TUCKER
Vice-President
M5 Marketing Communications Inc.

KEN MARSHALL
President
Rogers Cable - Atlantic Region

OFFICERS

DEAN T. MacDONALD
Chairman

EDMUND J. MARTIN
President and Chief Executive Officer

JAMES R. HAYNES
Vice-President, Regulated Operations

FRED H. MARTIN
Vice-President, Engineering Services

JIM KEATING
Vice-President, Business Development

WAYNE CHAMBERLAIN
General Counsel and Corporate Secretary

PETER A. HICKMAN
Assistant Corporate Secretary

MARK G.S. BRADBURY
Director, Finance

HEAD AND CORPORATE OFFICE
P.O. Box 12400
St. John's, Newfoundland and Labrador
A1B 4K7

NEWFOUNDLAND AND LABRADOR HYDRO
NON-CONSOLIDATED BALANCE SHEET

As at December 31 (millions of dollars)

	2005	2004
ASSETS		
Capital assets (Note 3)		
Capital assets in service	1,939.1	1,922.4
Less contributions in aid of construction	<u>84.6</u>	<u>85.1</u>
	1,854.5	1,837.3
Less accumulated depreciation	<u>506.4</u>	<u>481.8</u>
	1,348.1	1,355.5
Construction in progress	<u>62.2</u>	<u>52.2</u>
	<u>1,410.3</u>	<u>1,407.7</u>
Current assets		
Cash and cash equivalents	0.3	-
Short-term investments	0.5	-
Accounts receivable	57.2	56.0
Current portion of long-term receivable (Note 4)	41.7	40.1
Current portion of rate stabilization plan (Note 4)	0.1	8.6
Due from related party (Note 12)	-	0.2
Fuel and supplies at average cost	51.3	39.9
Prepaid expenses	<u>1.9</u>	<u>1.6</u>
	<u>153.0</u>	<u>146.4</u>
Sinking funds (Note 9)	85.8	72.6
Long-term receivable (Note 4)	63.2	93.9
Investments (Note 5)	324.1	312.1
Deferred charges (Notes 4 and 6)	<u>84.8</u>	<u>84.7</u>
	<u>2,121.2</u>	<u>2,117.4</u>

See accompanying notes

NEWFOUNDLAND AND LABRADOR HYDRO **NON-CONSOLIDATED BALANCE SHEET**

As at December 31 (millions of dollars)

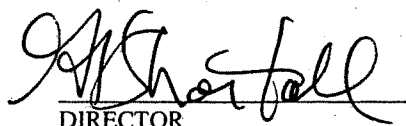
	2005	2004
LIABILITIES AND SHAREHOLDER'S EQUITY		
Long-term debt (Note 7)	<u>1,123.1</u>	<u>1,341.0</u>
Current liabilities		
Bank indebtedness	5.5	7.4
Accounts payable and accrued liabilities	49.3	40.8
Accrued interest	29.3	30.1
Long-term debt due within one year (Note 7)	208.4	13.8
Current portion of rate stabilization plan (Note 4)	1.3	-
Promissory notes (Note 7)	151.3	158.3
Due to related parties (Note 12)	<u>3.2</u>	<u>-</u>
	<u>448.3</u>	<u>250.4</u>
Rate stabilization plan (Note 4)	10.6	5.5
Employee future benefits (Note 8)	<u>32.3</u>	<u>29.7</u>
	<u>42.9</u>	<u>35.2</u>
Shareholder's equity		
Share capital		
Common shares of par value of \$1 each		
Authorized 25,000,000 shares; issued 22,503,942 shares	22.5	22.5
Contributed capital		
Lower Churchill Development (Note 5)	15.4	15.4
Muskrat Falls Project	2.2	2.2
Retained earnings	<u>466.8</u>	<u>450.7</u>
	<u>506.9</u>	<u>490.8</u>
Commitments and contingencies (Note 11)	<u>2,121.2</u>	<u>2,117.4</u>

See accompanying notes

On behalf of the Board:



DIRECTOR



DIRECTOR

NEWFOUNDLAND AND LABRADOR HYDRO
NON-CONSOLIDATED STATEMENT OF INCOME AND RETAINED EARNINGS

<i>Year ended December 31 (millions of dollars)</i>	2005	2004
Revenue		
Energy sales	404.2	390.8
Recovery of costs in rate stabilization plan (Note 4)	56.5	34.2
Other	2.3	2.2
	<u>463.0</u>	<u>427.2</u>
Expenses		
Operations and administration (Note 12)	96.6	91.8
Fuels	84.5	83.1
Amortization of costs in rate stabilization plan (Note 4)	56.5	34.2
Power purchased (Note 12)	39.9	40.2
Depreciation	35.5	33.8
Interest (Note 10)	99.5	96.5
	<u>412.5</u>	<u>379.6</u>
Income from operations	<u>50.5</u>	<u>47.6</u>
Other revenue (expense)		
Equity in net income of CF(L)Co. (Note 5)	14.6	15.0
Preferred dividends from CF(L)Co.	9.1	6.9
Interest on share purchase debt (Note 10)	(2.3)	(2.3)
	<u>21.4</u>	<u>19.6</u>
Net income	71.9	67.2
Retained earnings, beginning of year	450.7	434.1
	522.6	501.3
Dividends	55.8	50.6
Retained earnings, end of year	<u>466.8</u>	<u>450.7</u>

See accompanying notes

NEWFOUNDLAND AND LABRADOR HYDRO **NON-CONSOLIDATED STATEMENT OF CASH FLOWS**

Year ended December 31 (millions of dollars)

2005

2004

Cash provided by (used in)

Operating activities

Net income	71.9	67.2
Adjusted for items not involving a cash flow		
Depreciation	35.5	33.8
Amortization of deferred charges	3.9	3.5
Equity in net income of CF(L)Co.	(14.6)	(15.0)
Rate stabilization plan	14.9	(3.1)
Loss on disposal of capital assets	3.7	1.8
	<u>115.3</u>	<u>88.2</u>

Change in non-cash balances related to operations

Accounts receivable	(1.2)	(11.4)
Fuel and supplies	(11.4)	0.8
Prepaid expenses	(0.3)	0.5
Long-term receivable	29.1	21.7
Accounts payable and accrued liabilities	10.8	0.5
Accrued interest	(0.8)	(0.1)
Due to related parties	3.4	(4.3)
Employee future benefits	2.6	2.8
	<u>147.5</u>	<u>98.7</u>

Dividends from CF(L)Co.

	<u>2.6</u>	<u>2.6</u>
	<u>150.1</u>	<u>101.3</u>

Financing activities

Long-term debt retired	(17.7)	(3.4)
Increase in sinking funds	(19.5)	(21.5)
(Decrease) increase in promissory notes	(7.0)	8.1
Dividends	(55.8)	(50.6)
	<u>(100.0)</u>	<u>(67.4)</u>

Investing activities

Net additions to capital assets	(41.5)	(35.0)
Proceeds on disposal of capital assets	0.4	1.0
Increase in short-term investments	(0.5)	-
(Additions) reductions to deferred charges	(4.0)	0.5
Change in accounts payable related to investing activities	(2.3)	(2.1)
	<u>(47.9)</u>	<u>(35.6)</u>

Net increase (decrease) in cash

Cash position, beginning of year

Cash position, end of year

	<u>2.2</u>	<u>(1.7)</u>
	<u>(7.4)</u>	<u>(5.7)</u>
	<u>(5.2)</u>	<u>(7.4)</u>

Cash position is represented by

Cash and cash equivalents	0.3	-
Bank indebtedness	(5.5)	(7.4)
	<u>(5.2)</u>	<u>(7.4)</u>

Supplementary disclosure of cash flow information

Interest paid	107.4	107.0
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See accompanying notes

NEWFOUNDLAND AND LABRADOR HYDRO

NOTES TO NON-CONSOLIDATED FINANCIAL STATEMENTS

Newfoundland and Labrador Hydro (Hydro) is incorporated under a special act of the Legislature of the Province of Newfoundland and Labrador (Province) as a Crown corporation and is exempt from paying income taxes under Section 149 (1)(d) of the Income Tax Act. The principal activity of Hydro is the development, generation and sale of electric power.

1. PRINCIPLES OF FINANCIAL STATEMENT PRESENTATION

These financial statements have been prepared in accordance with the significant accounting policies set out below. These financial statements materially differ from Canadian generally accepted accounting principles because they are non-consolidated. Hydro's investments in its subsidiary and jointly controlled companies have been accounted for using the equity method of accounting. Consolidated financial statements for the same period have been prepared for presentation to the Lieutenant-Governor in Council of the Province.

Preparation of these financial statements requires the use of estimates and assumptions that affect the amounts reported and disclosed in these statements and related notes. Actual results may differ from these estimates, including changes as a result of future decisions made by the Newfoundland and Labrador Board of Commissioners of Public Utilities (PUB).

2. SIGNIFICANT ACCOUNTING POLICIES

Rates and Regulations

Hydro's earnings from its electrical sales to most customers within the Province are subject to rate regulation. As well, Hydro's borrowing and capital expenditure programs are also subject to review and approval by the PUB, which as an agency of the Province, is a related party. Rates are set through periodic general rate applications utilizing a cost of service (COS) methodology. The allowed rate of return on rate base is 7.5%. The effects of rate regulation on the financial statements are more fully disclosed in Note 4.

Cash Equivalents and Short-Term Investments

Cash equivalents and short-term investments consist primarily of Canadian treasury bills and banker's acceptances. Those with original maturities at date of purchase of three months or less are classified as cash equivalents whereas those with original maturities beyond three months and less than twelve months are classified as short-term investments. Both are stated at cost, which approximates market value. There were short-term investments outstanding at December 31, 2005 (2004 - nil) bearing interest rates of 3.20% to 3.25% (2004 - nil) per annum.

Capital Assets and Depreciation

Expenditures for additions, improvements and renewals are capitalized and normal expenditures for maintenance and repairs are charged to operations.

Construction in progress includes the costs incurred in preliminary feasibility studies, engineering and construction of new generation, transmission and distribution facilities. Interest is charged to construction in progress at rates equivalent to the weighted average cost of capital.

During 2004, Hydro adopted the recommendations of the Canadian Institute of Chartered Accountants' (CICA) Handbook Section 3110, *Asset Retirement Obligations*. This new accounting standard requires that the company recognize the fair value of the future expenditures required to settle legal obligations associated with the retirement of capital assets, to the extent that it is reasonably estimable. As it is expected that Hydro's assets will be used for an indefinite period, no removal date can be determined and consequently, a reasonable estimate of the fair value of any related asset retirement obligation cannot be determined at this time. If it becomes possible to estimate the fair value of the cost of removing assets that Hydro is legally required to remove, an asset retirement obligation will be recognized at

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Capital Assets and Depreciation (cont'd.)

Contributions in aid of construction are funds received from customers and governments toward the cost of capital assets. Contributions are treated as a reduction to capital assets and the net capital assets are depreciated.

Depreciation is calculated on hydroelectric generating plant and on transmission plant in service on the sinking fund method using interest factors ranging from 5.25% to 15.79%. Depreciation on other plant in service is calculated on the straight-line method. These methods are designed to fully amortize the cost of the facilities, after deducting contributions in aid of construction, over their estimated service lives.

Estimated service lives of the major assets are as follows:

Generation Plant	
Hydroelectric	50, 75 and 100 years
Thermal	25 and 30 years
Diesel	20 years
Transmission	
Lines	40 and 50 years
Switching stations	40 years
Distribution system	30 years
Other	3 to 50 years

Debt Discount and Financing Expenses

These costs are amortized on a straight-line basis over the lives of the respective debt issues.

Promissory Notes

Promissory Notes bear interest from 2.85% to 3.68% per annum (2004 - 2.10% to 2.86%) with carrying value approximating fair value due to their short-term nature.

Revenue Recognition

Revenue is recognized on the accrual basis, as power and energy deliveries are made, and includes an estimate of the value of electricity consumed by customers in the year, but billed subsequent to year-end. During 2005, a regulated utility customer accounted for 61% (2004 - 60%) of energy sales revenue.

Foreign Currency Translation

Foreign currency transactions are translated into their Canadian dollar equivalent as follows:

- (a) At the transaction date, each asset, liability, revenue or expense is translated using exchange rates in effect at that date.
- (b) At each balance sheet date monetary assets and liabilities are adjusted to reflect exchange rates in effect at that date. Any resulting gain or loss is reflected in income.

Financial Instruments

From time to time, Hydro enters into interest rate swap agreements to manage interest rate risk. Net receipts or payments under the swap agreements are recorded as adjustments to interest expense.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Employee Future Benefits

Employees participate in the Province's Public Service Pension Plan, a multiemployer defined benefit plan. The employer's contributions are expensed as incurred.

Hydro provides group life insurance and health care benefits on a cost-shared basis to retired employees, in addition to a severance payment upon retirement. The expected cost of providing these other employee future benefits is accounted for on an accrual basis, and has been actuarially determined using the projected benefit method prorated on service and management's best estimate of salary escalation, retirement ages of employees, and expected health care costs. The excess of cumulative net actuarial gains and losses over 10% of the accrued benefit obligation are amortized over the expected average remaining service life of the employee group, which is approximately twelve years.

3. CAPITAL ASSETS

	Capital Assets in Service	Contributions In aid of Construction	Accumulated Depreciation	Construction In Progress
<i>millions of dollars</i>	2005			
Generation Plant				
Hydroelectric	838.0	20.5	42.6	0.1
Thermal	231.7	-	180.8	0.7
Diesel	58.5	6.2	26.0	0.1
Transmission and Distribution	632.2	55.1	149.4	2.2
Other	178.7	2.8	107.6	59.1
	<u>1,939.1</u>	<u>84.6</u>	<u>506.4</u>	<u>62.2</u>
	2004			
Generation Plant				
Hydroelectric	829.6	20.5	39.6	0.2
Thermal	228.1	-	177.4	-
Diesel	56.9	6.5	24.1	0.4
Transmission and Distribution	628.9	55.1	136.2	0.2
Other	178.9	3.0	104.5	51.4
	<u>1,922.4</u>	<u>85.1</u>	<u>481.8</u>	<u>52.2</u>

4. FINANCIAL STATEMENT EFFECTS OF RATE REGULATION

The following is a description of each of the circumstances in which rate regulation affects the accounting for a transaction or event. Regulatory assets represent future revenues associated with certain costs, incurred in current or prior periods, that are expected to be recovered from customers in future periods through the rate-setting process. Regulatory liabilities represent future reductions or limitations of increases in revenues associated with amounts that are expected to be refunded to customers as a result of the rate-setting process.

Capital Assets and Depreciation

The PUB permits an allowance for funds used during construction (AFUDC), based on Hydro's weighted average cost of capital, to be included in the cost of capital assets and depreciated over future periods as part of the total cost of the related asset. Since Hydro's AFUDC (7.6%) is lower than its cost of debt (8.0%), the amount capitalized is \$0.2 million (2004 - \$0.2 million) lower and interest expense is higher than that which would be permitted in the absence of rate regulation (Note 10).

4. FINANCIAL STATEMENT EFFECTS OF RATE REGULATION (cont'd.)

Capital Assets and Depreciation (cont'd.)

Hydro depreciates its hydroelectric generating assets and transmission assets using the sinking fund method, as approved by the PUB. In the absence of rate regulation, these assets would likely be depreciated using the straight-line method (Note 1).

During 2005, pursuant to Order No. P.U. 7 (2002-2003) Hydro engaged an independent consultant to conduct a depreciation study. The scope of this study included a review of Hydro's depreciation methods as well as a statistical analysis of service life estimates and calculation of appropriate depreciation rates and annual and accrued depreciation balances as at December 31, 2004. Based on the results of this study, management estimates that accumulated depreciation is approximately \$170-180 million lower than it would otherwise be, and annual depreciation expense is \$10-11 million lower, primarily due to the use of sinking fund rather than straight line depreciation for hydroelectric and transmission assets.

Rate Stabilization Plan and Related Long-Term Receivable

Fuel expenses are included in allowed rates on a forecast basis. On January 1, 1986, Hydro, having received the concurrence of the PUB, implemented a rate stabilization plan (RSP) which primarily provides for the deferral of fuel expense variances resulting from changes in fuel prices, levels of precipitation and load. Adjustments are required in retail rates to cover the amortization of the balance in the plan and are implemented on July 1 of each year. Similar adjustments required in industrial rates are implemented on January 1 of each year.

Pursuant to Order No. P.U. 7 (2002-2003) and Order No. P.U. 40 (2003) RSP balances which accumulated prior to December 31, 2003, have been converted to a long-term receivable which bears interest at the weighted average cost of capital and is to be recovered over a four-year period, which commenced in 2004. At December 31, 2005 the unamortized balance was \$104.9 million (2004 - \$134.0 million). Any subsequent balances accumulating in the RSP including financing charges, are to be recovered in the following year, with the exception of hydraulic variation, which will be recovered or refunded at a rate of twenty-five percent of the outstanding balance at year-end. Additionally, a fuel rider is calculated annually based on the forecast fuel price and is added to or subtracted from the rates that would otherwise be in effect.

Hydro recognizes the RSP balances as a regulatory asset or liability based on the expectation that rates will be adjusted annually to provide for the collection from, or refund to, customers in future periods. In the absence of rate regulation, generally accepted accounting principles would require that the cost of fuel be recognized as an operating expense in the period in which it was consumed. In 2005, \$6.3 million (2004 - \$5.9 million) was deferred in the RSP.

Foreign Exchange Losses

The PUB has accepted the inclusion of realized foreign exchange losses related to long-term debt in rates charged to customers in future periods. Any such loss, net of any gain, is deferred to the time of the next rate hearing for inclusion in the new rates to be set at that time. Accordingly, these losses are recognized as a regulatory asset. In the absence of rate regulation, generally accepted accounting principles would require that Hydro include the losses in operating costs, in each year that the related debt was outstanding to reflect the exchange rates in effect on each reporting date.

Commencing in 2002, the PUB ordered Hydro's deferred realized foreign exchange losses, be amortized over a forty-year period. This amortization, of \$2.2 million annually, is included in interest expense (Notes 6 and 10).

Deferred Regulatory Costs

Pursuant to Order No. P.U. 14 (2004), the PUB approved the deferral of external costs associated with the general rate application and hearing, to be amortized over a 3 year period, which commenced in 2004. These costs are recognized as a regulatory asset. In the absence of rate regulation, generally accepted accounting principles would require that Hydro include these costs in operating costs in the year in which they were incurred. In 2005, \$0.7 million (2004 - \$0.4 million) of amortization was recognized in operations and administration expenses (Note 6).

4. FINANCIAL STATEMENT EFFECTS OF RATE REGULATION (cont'd.)

Deferred Major Extraordinary Repair

In its report dated April 13, 1992, the PUB recommended that Hydro adopt a policy of deferring and amortizing the costs of major extraordinary repairs in excess of \$500,000, subject to PUB approval on a case-by-case basis. In 2005, Hydro started an asbestos abatement program at the Holyrood Thermal Generating Station. This program is to be carried out over a three-year period, which commenced in 2005. Pursuant to Order P.U. No. 2 (2005) the PUB approved the deferral and amortization of these costs as a major extraordinary repair. Accordingly, the costs incurred in each year of the program will be recognized as a regulatory asset which will be amortized over the subsequent five-year period. In the absence of rate regulation, generally accepted accounting principles would require that Hydro expense the cost of the asbestos abatement program in the year in which they were incurred. In 2005, \$0.1 million (2004 - nil) of amortization was recognized in operating costs, and \$3.9 million (2004 - nil) was deferred in relation to the asbestos abatement program (Note 6).

Deferred Study Costs

Pursuant to Order No. P.U. 14 (2004) the PUB directed Hydro to conduct an independent study of the treatment of Newfoundland Power's generation in Hydro's COS, and an independent marginal cost study, and to accumulate these costs in a deferral account to be dealt with at the next general rate application (planned for 2006). Hydro intends to seek, and expects to receive, approval for recovery of these costs over a three year period commencing in 2007. Accordingly, these costs, in the amount of \$0.1 million, have been recognized as a regulatory asset. In the absence of rate regulation, generally accepted accounting principles would require that Hydro include the cost of these studies in operating costs in the year in which they were incurred (Note 6).

Deferred Purchased Power Savings

In 1997, Hydro interconnected communities in the area of L'Anse au Clair to Red Bay to the Hydro Quebec system. In its report dated July 12, 1996, the PUB recommended that Hydro defer the benefits of a reduced initial purchased power rate, to be amortized over a 30-year period. These savings are recognized as a regulatory liability. In the absence of rate regulation, generally accepted accounting principles would require that Hydro include the actual cost of purchased power in operating costs in the year in which they were incurred. At December 31, 2005 the unamortized balance was \$0.8 million, (2004 - \$0.8 million) and is included in accounts payable and accrued liabilities.

5. INVESTMENTS

<i>millions of dollars</i>	Ownership Interest	2005	2004	
Churchill Falls (Labrador) Corporation Limited	65.8%			
Shares, at cost		167.2	167.2	
Equity in retained earnings at beginning of year		142.2	129.8	
Equity in net income for the year		14.6	15.0	
Dividends for the year		(2.6)	(2.6)	
		<u>321.4</u>	<u>309.4</u>	(a)
Lower Churchill Development Corporation Limited	51.0%	2.7	2.7	(b)
Gull Island Power Company Limited	100.0%	-	-	(c)
		<u>324.1</u>	<u>312.1</u>	

(a) A portion of Hydro's shareholding in CF(L)Co. is deposited in a voting trust pursuant to an agreement with Hydro-Québec.

5. INVESTMENTS (cont'd.)**(a) (cont'd.)**

Effective June 18, 1999, the two shareholders of CF(L)Co., Hydro and Hydro-Québec, entered into a shareholders' agreement which provided, among other matters, that certain of the strategic operating, financing and investing policies of CF(L)Co. be subject to approval jointly by representatives of Hydro and Hydro-Québec. CF(L)Co. also receives certain benefits from Hydro-Québec, including significant revenues from Hydro-Québec under a guaranteed winter availability contract through 2041.

- (b) The Lower Churchill Development Corporation Limited (LCDC) was established with the objective of developing all or part of the hydroelectric potential of the Lower Churchill River (Lower Churchill Development) in Labrador.

Hydro, the designate for the Province's shareholding in LCDC, holds 1,540 Class A common shares of LCDC. 520 shares were acquired in 1979 pursuant to the signing of an Option Agreement between LCDC and the Province, dated November 24, 1978, and expiring November 24, 2006. 510 shares were acquired in each of the years 1980 and 1981, by way of capital contributions from the Province.

- (c) Gull Island Power Company Limited (GIPCo.) is incorporated under the laws of Canada. Its objective was to develop the hydroelectric potential at Gull Island on the Lower Churchill River in Labrador, and construct a direct current transmission system from Labrador to the island of Newfoundland (Gull Island Project). All project costs were funded by way of capital contributions from the Province. Hydro suspended all work on the Gull Island Project in 1976, in the absence of satisfactory arrangements for the financing of the project and the marketing of available power.

Upon agreement to continue with the Lower Churchill Development, LCDC has the option to purchase the GIPCo. assets pursuant to the provisions of the Option Agreement.

6. DEFERRED CHARGES

<i>millions of dollars</i>	2005	2004
Debt discount, financing expenses and other	10.1	10.1
Accumulated amortization	<u>7.6</u>	<u>6.6</u>
	<u>2.5</u>	<u>3.5</u>
Regulatory costs	1.8	1.8
Major extraordinary repair	3.9	-
Study costs	<u>0.1</u>	-
	<u>5.8</u>	<u>1.8</u>
Accumulated amortization	<u>1.2</u>	<u>0.4</u>
	<u>4.6</u>	<u>1.4</u>
Net Foreign exchange losses realized	86.3	86.3
Accumulated amortization	<u>8.6</u>	<u>6.5</u>
	<u>77.7</u>	<u>79.8</u>
Net deferred charges	<u>84.8</u>	<u>84.7</u>

7. LONG-TERM DEBT

Series	Interest Rate %	Year of Issue	Year of Maturity	2005	2004
<i>millions of dollars</i>					
AC	5.05	2001	2006	200.0	200.0
AA	5.50	1998	2008	200.0	200.0
V	10.50	1989	2014	125.0	125.0 (a)
X	10.25	1992	2017	150.0	150.0 (a)
Y	8.40	1996	2026	300.0	300.0 (a)
AB	6.65	2001	2031	300.0	300.0 (a)
AD	5.70	2003	2033	125.0	125.0 (a)
Total debentures				1,400.0	1,400.0
Less sinking fund investments in own debentures				69.2	62.8
				1,330.8	1,337.2
Government of Canada loans at 5.25% to 5.63% maturing in 2006 to 2014				0.1	16.4
Other				0.6	1.2
				1,331.5	1,354.8
Less payments due within one year				208.4	13.8
				<u>1,123.1</u>	<u>1,341.0</u>

(a) Sinking funds have been established for these issues.

Promissory notes, debentures and long-term loans are unsecured and unconditionally guaranteed as to principal and interest and where applicable, sinking fund payments, by the Province. The Province charges Hydro a guarantee fee of one percent annually on the total debt (net of sinking funds) guaranteed by the Province, outstanding as of the preceding December 31.

Required repayments of long-term debt and sinking fund requirements over the next five years will be as follows:

<i>millions of dollars</i>	2006	2007	2008	2009	2010
	208.4	8.3	208.3	8.3	8.2

The payments due within one year include sinking fund requirements of \$8.2 million (2004 - \$10.0 million).

8. EMPLOYEE FUTURE BENEFITS

Pension Plan

Employees participate in the Province's Public Service Pension Plan, a multiemployer defined benefit plan. The employer's contributions of \$3.4 million (2004 - \$3.4 million) are expensed as incurred.

8. EMPLOYEE FUTURE BENEFITS (cont'd.)

Other Benefits

Additionally, Hydro provides group life insurance and healthcare benefits on a cost-shared basis to retired employees, and in certain cases, their surviving spouses, in addition to a severance payment upon retirement. The most recent actuarial valuation was performed as at December 31, 2004.

<i>millions of dollars</i>	2005	2004
Accrued benefit obligation		
Balance at beginning of year	39.3	33.6
Current service cost	1.4	1.3
Interest cost	2.5	2.4
Actuarial loss	-	3.5
Benefits paid	(1.8)	(1.5)
Balance at end of year	<u>41.4</u>	<u>39.3</u>
Plan deficit	41.4	39.3
Unamortized actuarial loss	(8.8)	(9.3)
Unamortized past-service cost	(0.3)	(0.3)
Accrued benefit liability at end of year	<u>32.3</u>	<u>29.7</u>

<i>millions of dollars</i>	2005	2004
Current service cost	1.4	1.3
Interest cost	2.5	2.4
Actuarial losses	-	3.5
	<u>3.9</u>	<u>7.2</u>
Adjustments		
Difference between actual actuarial loss and amount recognized	0.5	(2.9)
Benefit expense	<u>4.4</u>	<u>4.3</u>

The significant actuarial assumptions used in measuring the company's accrued benefit obligations and benefit expense are as follows:

	2005	2004
Discount rate	6.3%	6.3%
Rate of compensation increase	3.5%	3.5%
Assumed healthcare trend rates:		
	2005	2004
Initial healthcare expense trend rate	12.0%	12.0%
Cost trend decline to	5.0%	5.0%
Year that rate reaches the rate it is assumed to remain at	2010	2010

9. FINANCIAL INSTRUMENTS

Fair Value

The estimated fair values of financial instruments as at December 31, 2005 and 2004 are based on relevant market prices and information available at the time. The fair value of long-term debt is estimated based on the quoted market price for the same or similar debt instruments. The fair value estimates below are not necessarily indicative of the amounts that Hydro might receive or incur in actual market transactions. As a significant number of Hydro's assets and liabilities, including fuels and supplies and capital assets, do not meet the definition of financial instruments, the fair value estimates below do not reflect the fair value of Hydro as a whole.

	Carrying Value	Fair Value	Carrying Value	Fair Value
<i>millions of dollars</i>	2005		2004	
Financial Assets				
Sinking funds	85.8	102.0	72.6	81.0
Financial Liabilities				
Long-term debt including amount due in one year	1,331.5	1,712.3	1,354.8	1,663.6

Cash and cash equivalents, short-term investments, accounts receivable, bank indebtedness, accounts payable, accrued interest, promissory notes and due to related parties, are all short-term in nature and as such their carrying value approximates fair value. At December 31, 2005 approximately 62.1% (2004 - 62.2%) of the total accounts receivable balance outstanding is due from a regulated utility.

Sinking Funds

Sinking fund investments consist of bonds, debentures, promissory notes and coupons issued by, or guaranteed by, the Government of Canada or any province of Canada, and have maturity dates ranging from 2013 to 2033. Hydro debentures which Management intends to hold to maturity are deducted from long-term debt while all other sinking fund investments are shown separately on the balance sheet as assets. Annual contributions to the various sinking funds are as per bond indenture terms, and are structured to ensure the availability of adequate funds at the time of expected bond redemption. Effective yields range from 4.50% to 9.86% (2004 - 4.77% to 9.86%).

10. INTEREST EXPENSE

<i>millions of dollars</i>	2005	2004
Gross interest		
Long-term debt	102.4	103.1
Promissory notes	4.5	4.1
	106.9	107.2
Amortization of debt discount and financing expenses	1.0	1.0
Amortization of foreign exchange losses	2.3	2.2
	110.2	110.4
Less		
Interest capitalized during construction	4.3	3.6
Interest earned	18.5	22.6
	87.4	84.2
Less		
Interest attributable to CF(L)Co. share purchase debt	2.3	2.3
Net interest attributable to Hydro	85.1	81.9
Debt guarantee fee	14.4	14.6
Net interest and guarantee fee	99.5	96.5

11. COMMITMENTS AND CONTINGENCIES

- (a) Hydro has received claims instituted by various companies and individuals with respect to outages and other miscellaneous matters. The aggregate of these claims, less any amounts that have been provided for in Hydro's financial statements is approximately \$0.5 million (2004 - \$7.7 million). The final resolution of these matters is currently under negotiation.

Legal proceedings have been commenced against Hydro by one of its customers claiming approximately \$22.2 million related to outages and plant shutdowns. Hydro is defending this claim and Management believes that this claim will not be successful.

- (b) Outstanding commitments for capital projects total approximately \$13.1 million at December 31, 2005 (2004 - \$5.7 million).

12. RELATED PARTY TRANSACTIONS

<i>millions of dollars</i>	2005	2004
Due to GIPCo. - promissory notes at 3.00% (2004 - 2.65%)	0.1	0.1
Due to (from) CF(L)Co. - other	3.1	(0.3)
	<u>3.2</u>	<u>(0.2)</u>

- (a) Hydro has entered into a long-term power contract with CF(L)Co. for the purchase of \$6.1 million (2004 - \$6.2 million) of the power produced by CF(L)Co.
- (b) Under an agreement between Hydro and CF(L)Co., Hydro provides certain engineering, technical, management and administrative services to CF(L)Co. These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties. For the year ended December 31, 2005 the fees paid to Hydro for these services amounted to approximately \$2.2 million (2004 - \$2.1 million).

13. SUBSEQUENT EVENTS

In January 2006, Hydro applied to Hydro-Quebec TransEnergie for transmission service to transmit Lower Churchill power from the Labrador/Quebec border into Quebec and other markets. Hydro-Quebec will conduct an initial assessment and detailed engineering studies to determine feasibility. Hydro's deposit of \$17.2 million is refundable if the application is rejected or withdrawn prior to entering into a service agreement.

14. COMPARATIVE FIGURES

Certain of the 2004 comparative figures have been reclassified to conform with the 2005 financial statement presentation.

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Newfoundland and Labrador Hydro Computation of Rate Base (\$ 000s)		
Year Ended December 31		
	2005	2004
Capital Assets - Return 4	1,939,115	1,922,374
<u>Deduct:</u>		
Accumulated Depreciation - Return 6	506,391	481,801
Contributions in Aid of Construction - Return 7	84,627	85,081
Assets Not in Service / Non Regulated	2,138	2,153
	<u>593,156</u>	<u>569,035</u>
Net Capital Assets	<u>1,345,959</u>	<u>1,353,339</u>
Net Capital Assets, Previous Year	<u>1,353,339</u>	<u>1,360,754</u>
Average Capital Assets	1,349,649	1,357,047
Cash Working Capital Allowance - Return 8	2,711	2,943
Fuel Inventory - Return 10	21,506	15,611
Supplies Inventory - Return 10	20,084	18,615
Average Deferred Foreign Exchange and PUB Costs - Return 11	<u>79,809</u>	<u>82,506</u>
Average Rate Base at Year-End - Return 12	<u><u>1,473,759</u></u>	<u><u>1,476,722</u></u>

Newfoundland and Labrador Hydro Plant Investment (\$ 000s)					
	Balance 1-Jan-05	Adjustments During 2005	Additions During 2005	Retirements During 2005	Balance 31-Dec-05
Power Generation					
Steam	182,695	32	3,111	-	185,838
Hydro	829,627	3,525	7,260	(2,390)	838,022
Diesel	56,851	389	2,476	(1,270)	58,446
Gas turbine	45,384	-	520	(53)	45,851
	1,114,557	3,946	13,367	(3,713)	1,128,157
Substations	173,765	(4,046)	1,186	(1,885)	169,020
Transmission	309,551	160	2,708	(608)	311,811
Distribution	145,625	57	7,514	(1,768)	151,428
General plant	91,927	(1,424)	3,368	(4,726)	89,145
Telecontrol	65,594	1,019	4,427	(2,781)	68,259
Computer software	15,121	41	855	(45)	15,972
Other	2,413	-	93	(1,004)	1,502
Total depreciable plant	1,918,553	(247)	33,518	(16,530)	1,935,294
Non depreciable land	3,821	-	-	-	3,821
Plant investment - Return 3	<u>1,922,374</u>	<u>(247)</u>	<u>33,518</u>	<u>(16,530)</u>	<u>1,939,115</u>
Work in progress					62,226
Total plant investment					<u><u>2,001,341</u></u>

Newfoundland and Labrador Hydro
Capital Expenditures - Overview
(\$ 000s)

Year Ended December 31

	<u>Annual Budget 2005</u>	<u>Total Actual Expenditures 2005</u>	<u>Variance From 2005 Budget</u>
Generation	7,779	7,386	(393)
Transmission and Rural Operations	19,753	15,991	(3,762)
General Properties	15,920	7,909	(8,011)
Allowance for Unforeseen Events	1,000	103	(897)
Projects Approved by PUB	3,112	2,477	(635)
New Projects Less than \$50,000 Approved by Hydro	196	86	(110)
 Total Capital Budget	 <u>47,760</u>	 <u>33,952</u>	 <u>(13,808)</u>
 Approved P.U. 53 (2004)	 42,431		
Approved P.U. 3 (2005) / P.U. 12 (2005)	5,826		
Approved P.U. 3 (2005) / P.U. 12 (2005)	(5,826)		
Carryover Projects 2004 to 2005	1,778		
Approved P.U. 11 (2005)	3,154		
Approved P.U. 14 (2005)	991		
Approved P.U. 24 (2005)	(790)		
Approved P.U. 29 (2005)	172		
Approved P.U. 29 (2005)	(172)		
New projects under \$50,000 Approved by Hydro	196		
Total Approved Capital Budget	<u>47,760</u>		

Newfoundland and Labrador Hydro Accumulated Depreciation (\$ 000s)			
Balance, January 1, 2005			481,801
<u>Add:</u>			
Depreciation	35,493		
Adjustments	<u>(97)</u>		
			35,396
<u>Deduct:</u>			
Retirements			10,806
Balance, December 31, 2005 - Return 3			<u><u>506,391</u></u>
Depreciation Rates - 2005			
Steam - SL			6.45%
Hydro - SL			3.33%
Hydro - SF			7.57%
Gas Turbine - SL			4.00%
Diesel - SL			5.00%
Substations - SL			3.33%
Substations - SF			7.57%
Transmission - SL			3.33%
Transmission - SF			7.57%
Distribution - SL			3.33%
General Properties - SL	2.00%	-	33.33%
Telecontrol - SL	10.00%	or	20.00%
Software - SL			20.00%
Computer Hardware - SL	10.00%	or	33.33%
Percentage of accumulated depreciation to total depreciable plant			26.39%
Percentage of current depreciation to total depreciable plant			1.85%
Note: SL = straight-lined SF = sinking fund			

Newfoundland and Labrador Hydro Contributions in Aid of Construction (\$ 000s)			
	<u>CUSTOMERS</u>	<u>SHAREHOLDER</u>	<u>TOTAL</u>
Gross Contributions January 1, 2005	13,854	71,227	85,081
2005 Retirements	(215)	(1,258)	(1,473)
2005 Additions	<u>1,019</u>	<u>-</u>	<u>1,019</u>
Balance December 31, 2005 - Return 3	<u>14,658</u>	<u>69,969</u>	<u>84,627</u>

Newfoundland and Labrador Hydro Working Capital (\$ 000s)		
Year Ended December 31		
	<u>2005</u>	<u>2004</u>
Calculation of Cash Working Capital Allowance		
Operating Expenses for the Year - Return 9	93,284	88,978
Deduct: Non Regulated Expenses	<u>293</u>	<u>250</u>
	92,991	88,728
Add: Power Purchases	<u>36,191</u>	<u>35,343</u>
Total	<u><u>129,182</u></u>	<u><u>124,071</u></u>
Working Capital Allowance (Total x 4.71% ; 2004 - 4.96%)	6,084	6,154
Deduct: HST Adjustment	<u>3,373</u>	<u>3,211</u>
Working Capital Allowance - Return 3	<u><u>2,711</u></u>	<u><u>2,943</u></u>
In general, the Company's billing and collection procedures are consistent with those in place during the preceding year.		

Newfoundland and Labrador Hydro		
Statement of Operating Costs		
(\$ 000s)		
Year Ended December 31		
	<u>2005</u>	<u>2004</u>
Net operating		
Salaries and fringe benefits	56,077	56,521
System equipment maintenance	21,553	17,416
Office supplies and expenses	1,952	1,858
Professional services	4,271	3,652
Insurance	1,678	1,682
Equipment rentals	1,129	1,274
Travel	2,394	2,243
Miscellaneous expenses	3,751	3,784
Building rental and maintenance	785	775
Transportation	1,660	1,808
Customer costs	842	811
Cost recoveries	<u>(2,808)</u>	<u>(2,846)</u>
Subtotal - Return 8	93,284	88,978
Loss on disposal of capital assets	<u>3,291</u>	<u>2,839</u>
Total operating costs	<u><u>96,575</u></u>	<u><u>91,817</u></u>

Newfoundland & Labrador Hydro
Significant Operating Expense Variances
(\$ 000s)

	<u>2005</u>	<u>2004</u>	<u>Increase (Decrease)</u>
System Maintenance	21,553	17,416	4,137

The increase in this category of expenses was mainly due to higher maintenance costs at the Holyrood Thermal Plant (associated with a major overhaul of Unit #2 in 2005), Happy Valley Gas Turbine, isolated diesel plants and North Plant, Goose Bay.

Professional Services	4,271	3,652	619
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The increase in Professional Services category is mainly due to higher costs related to hiring and placement services and increased PUB related costs.

Loss on Disposal of Capital Assets	3,291	2,839	452
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The Loss on Disposal of Capital Assets was higher in 2005 due to adjustments necessitated as a result of findings from a conversion effort to merge the financial and maintenance asset records.

Newfoundland and Labrador Hydro
Fuel and Supplies Inventory
(\$ 000s)

Year Ended December 31

	Fuel		Supplies	
	2005	2004	2005	2004
Opening Balance	20,175	21,024	19,210	18,309
January	17,976	10,701	19,607	18,303
February	12,986	13,874	19,675	18,492
March	30,238	19,028	19,917	18,536
April	24,415	17,280	20,155	18,517
May	23,296	13,469	20,046	18,378
June	23,719	12,657	20,097	18,407
July	19,544	12,421	20,050	18,455
August	16,936	9,295	20,264	18,843
September	12,848	13,651	20,482	18,798
October	22,123	16,634	20,385	18,781
November	25,207	22,730	20,592	18,971
December	30,116	20,175	20,614	19,210
13 Month Average - Return 3	<u>21,506</u>	<u>15,611</u>	<u>20,084</u>	<u>18,615</u>

Newfoundland and Labrador Hydro Deferred Charges (\$ 000s)		
As at December 31		
	2005	2004
Unamortized debt discount, financing expenses and other	7,133	4,836
Foreign exchange losses realized	77,650	79,807
Total deferred charges, per financial statements	84,783	84,643
Deduct:		
Unamortized debt discount, financing expenses and other	7,133	4,836
Add:		
Unamortized PUB costs	720	1,440
Deferred Charges for Rate Base, end of current year	78,370	81,247
Deferred Charges for Rate Base, end of prior year	81,247	83,764
Average Deferred Charges for Rate Base - Return 3	79,809	82,506

Newfoundland and Labrador Hydro Return on Rate Base (\$ 000s)		
Year Ended December 31		
	<u>2005</u>	<u>2004</u>
(a) Corporate Net Income - Return 1	71,961	67,170
Deduct: Unregulated Earnings	<u>68,639</u>	<u>59,849</u>
Regulated Net Income	3,322	7,321
Add: Interest - Return 16	<u>99,479</u>	<u>96,527</u>
(b) Regulated Earnings	<u><u>102,801</u></u>	<u><u>103,848</u></u>
(c) Average Rate Base - Return 3	<u><u>1,473,759</u></u>	<u><u>1,476,722</u></u>
(d) Rate of Return on Average Rate Base	<u><u>6.98%</u></u>	<u><u>7.03%</u></u>

Newfoundland and Labrador Hydro Return on Regulated Average Retained Earnings (\$ 000s)			
Year Ended December 31			
		<u>2005</u>	<u>2004</u>
Regulated Retained Earnings			
Ending Retained Earnings As Per Balance Sheet		466,832	450,628
Deduct: Non-Regulated Retained Earnings			
Beginning Non-Regulated Retained Earnings	239,616		229,122
Non-Regulated Net Income for the year	68,639		59,849
Non-Regulated Dividends for the year	(53,953)		(49,355)
Ending Non-Regulated Retained Earnings		<u>254,302</u>	<u>239,616</u>
Regulated Retained Earnings, end of year		<u><u>212,530</u></u>	<u><u>211,012</u></u>
Regulated Retained Earnings, beginning of year		<u><u>211,012</u></u>	<u><u>204,927</u></u>
Regulated Average Retained Earnings		<u><u>211,771</u></u>	<u><u>207,970</u></u>
Earnings Applicable to Retained Earnings - Return 1		71,961	67,170
Deduct: Non-Regulated Net Income		<u>68,639</u>	<u>59,849</u>
Regulated Earnings		<u><u>3,322</u></u>	<u><u>7,321</u></u>
Rate of Return on Regulated Average Retained Earnings		<u><u>1.57%</u></u>	<u><u>3.52%</u></u>

**Newfoundland and Labrador Hydro
Capital Structure
(\$ 000s)**

Year Ended December 31

Corporate

	2005		2004		Average	
	Amount	Percent	Amount	Percent	Amount	Percent
Debt (Note 1)	1,371,694	85.04%	1,410,998	85.69%	1,391,346	85.37%
Employee Future Benefits	32,266	2.00%	29,715	1.80%	30,991	1.90%
Retained Earnings - Hydro	209,098	12.96%	205,933	12.51%	207,516	12.73%
	<u>1,613,058</u>	<u>100.00%</u>	<u>1,646,646</u>	<u>100.00%</u>	<u>1,629,853</u>	<u>100.00%</u>

Regulated

	2005		2004		Average	
	Amount	Percent	Amount	Percent	Amount	Percent
Debt	1,313,584	84.29%	1,357,457	84.94%	1,335,521	84.62%
Employee Future Benefits	32,266	2.07%	29,715	1.86%	30,991	1.96%
Retained Earnings	212,530	13.64%	211,012	13.20%	211,771	13.42%
	<u>1,558,380</u>	<u>100.00%</u>	<u>1,598,184</u>	<u>100.00%</u>	<u>1,578,283</u>	<u>100.00%</u>

Note 1: Debt is the total debt per Return 15 with the Unamortized Debt Discount and Issue Expenses added back.

Newfoundland and Labrador Hydro			
Cost of Debt			
(\$ 000s)			
Year Ended December 31			
Corporate			
	<u>2005</u>	<u>2004</u>	<u>Average</u>
Long-Term Debt	1,331,626	1,354,811	1,343,219
Promissory Notes	151,295	158,285	154,790
Promissory Notes - Related Party	3,085	85	1,585
Sinking Funds	(85,841)	(72,669)	(79,255)
CF(L)Co Share Purchase Debt	(28,471)	(29,514)	(28,993)
Unamortized Debt Discount and Issue Expenses	<u>(6,413)</u>	<u>(3,396)</u>	<u>(4,905)</u>
Total Debt - Return 14	<u>1,365,281</u>	<u>1,407,602</u>	<u>1,386,442</u>
Interest Expense - 2005 Return 16			<u>112,234</u>
Cost of Debt			<u>8.10%</u>

Newfoundland and Labrador Hydro		
Interest Expense		
(\$ 000s)		
Year Ended December 31		
	2005	2004
Gross Interest		
Long-Term Debt	102,356	103,100
Promissory Notes	4,533	4,131
	<u>106,889</u>	<u>107,231</u>
Amortization of Debt Discount and Financing Expenses	917	996
Provision for Foreign Exchange	2,291	2,159
Interest Earned	(10,004)	(12,018)
Debt Guarantee Fee - Hydro	14,394	14,587
Deduct: Interest Attributable to CF(L)Co	<u>(2,253)</u>	<u>(2,295)</u>
Interest for Cost of Debt - Return 15	112,234	110,660
Deduct:		
Interest capitalized during construction	(4,296)	(3,595)
Interest earned on RSP	<u>(8,459)</u>	<u>(10,538)</u>
Net Interest Per Financial Statements - Return 1, 12	<u><u>99,479</u></u>	<u><u>96,527</u></u>

Newfoundland and Labrador Hydro Rate Stabilization Account - December 31, 2003 Plan (\$ 000s)					
Year Ended December 31					
Month	Utility		Industrial		Closing Balance
	Recovery	Interest	Recovery	Interest	
December 2004					133,933 ¹
January	(3,458)	620	(845)	197	130,447
February	(2,867)	603	(820)	193	127,556
March	(2,981)	589	(920)	189	124,433
April	(2,379)	574	(831)	185	121,982
May	(2,001)	563	(793)	181	119,932
June	(1,735)	554	(742)	177	118,186
July	(1,723)	547	(833)	173	116,350
August	(1,734)	540	(873)	169	114,452
September	(1,780)	533	(869)	165	112,501
October	(2,196)	525	(797)	161	110,194
November	(2,561)	515	(510)	157	107,795
December	(3,130)	503	(456)	155	104,867
	<u>(28,545)</u>	<u>6,666</u>	<u>(9,289)</u>	<u>2,102</u>	
1. The opening balance for industrial customers includes an increase of \$ 5,054 to reflect the effect on prior years balances of billing adjustments on January's bill relating to Abitibi Grand Falls and Stephenville for the period July to December 2004.					

Newfoundland and Labrador Hydro
Rate Stabilization Account - January 2004 to December 2005 Plan
(\$ 000s)

Year Ended December 31

Month	Utility						Industrial				
	Load Variation	Allocation Fuel Variation	Allocation Rural Rate Alteration	Financing Charges	Adjustment	Cumulative Net Balance	Load Variation	Allocation Fuel Variation	Financing Charges	Adjustment	Cumulative Net Balance
December 2004						4,910,867 ¹					3,712,142 ¹
January	156,874	(487,528)	(165,267)	29,948	(536,508)	3,908,386	(100,918)	(136,044)	22,638	(524,533)	2,973,285
February	(100,964)	410,414	(138,281)	23,835	(444,797)	3,658,593	(8,158)	114,532	18,132	(508,577)	2,589,214
March	408	1,452,305	(120,103)	22,311	(462,469)	4,551,045	131,796	406,545	15,790	(570,774)	2,572,571
April	(9,652)	1,163,341	(121,083)	27,754	(369,064)	5,242,341	(17,433)	319,648	15,688	(515,778)	2,374,696
May	34,039	253,406	(104,331)	31,970	(310,433)	5,146,992	30,298	60,554	14,482	(492,173)	1,987,857
June	(11,471)	87,303	(131,903)	31,388	(269,236)	4,853,073	(275,952)	15,881	12,123	(460,298)	1,279,611
July	430	908,328	(140,432)	29,596	(1,378,897)	4,272,098	(97,263)	237,445	7,803	(516,843)	910,753
August	(5,409)	459,002	(221,153)	26,053	(1,387,887)	3,142,704	3,716	116,722	5,554	(541,950)	494,795
September	(3,681)	798,506	(213,613)	19,165	(1,424,899)	2,318,182	162,625	215,033	3,017	(539,055)	336,415
October	17,171	2,095,571	(212,261)	14,137	(1,757,058)	2,475,742	49,091	543,057	2,052	(494,318)	436,297
November	97,090	2,961,131	(238,037)	15,098	(2,049,631)	3,261,393	(801,198)	693,829	2,661	(316,328)	15,261
December	126,365	2,867,191	(256,759)	19,889	(2,505,058)	3,513,021	(808,617)	620,173	93	(283,333)	(456,423)
Year to date	<u>301,200</u>	<u>12,968,970</u>	<u>(2,063,223)</u>	<u>291,144</u>	<u>(12,895,937)</u>	<u>(1,397,846)</u>	<u>(1,732,013)</u>	<u>3,207,375</u>	<u>120,033</u>	<u>(5,763,960)</u>	<u>(4,168,565)</u>
Hydraulic Allocation						<u>(3,393,171)</u>					<u>(839,170)</u>
Total						<u>119,850</u>					<u>(1,295,593)</u>
						To Return 18a					To Return 18a

¹ The Utility opening balance includes an increase of \$892 from \$4,909,975 and the Industrial opening balance includes a decrease of \$12,395 from \$ 3,724,537. The increase in Utility and the decrease in Industrial is the effect on prior years balances of billing adjustments on January's bill relating to Abitibi Grand Falls and Stephenville for the period July to December 2004.

Newfoundland and Labrador Hydro
Rate Stabilization Account - January 2004 to December 2005 Plan
(\$ 000s)

Year Ended December 31

Month	Hydraulic			From Return 18		Cumulative Net Balance
	Net Hydraulic Production Variation	Financing Charges	Cumulative Variation and Financing Charges	Utility Balance	Industrial Balance	
December 2004			(5,521,528)	4,910,867 ¹	3,712,142 ¹	3,101,481
January	(3,084,930)	(33,672)	(8,640,130)	3,908,386	2,973,285	(1,758,459)
February	2,366,583	(52,690)	(6,326,237)	3,658,593	2,589,214	(78,430)
March	848,600	(38,580)	(5,516,217)	4,551,045	2,572,571	1,607,399
April	(2,215,386)	(33,640)	(7,765,243)	5,242,341	2,374,696	(148,206)
May	(4,565,271)	(47,355)	(12,377,869)	5,146,992	1,987,857	(5,243,020)
June	(2,436,083)	(75,484)	(14,889,436)	4,853,073	1,279,611	(8,756,752)
July	3,525,485	(90,801)	(11,454,752)	4,272,098	910,753	(6,271,901)
August	1,586,839	(69,855)	(9,937,768)	3,142,704	494,795	(6,300,269)
September	(678,581)	(60,604)	(10,676,953)	2,318,182	336,415	(8,022,356)
October	(2,154,235)	(65,112)	(12,896,300)	2,475,742	436,297	(9,984,261)
November	907,754	(78,646)	(12,067,192)	3,261,393	15,261	(8,790,538)
December	(2,746,506)	(73,590)	(14,887,288)	3,513,021	(456,423)	(11,830,690)
Year to date	(8,645,731)	(720,029)	(9,365,760)			
Hydraulic Allocation	3,541,815	720,029	4,261,844	(3,393,171)	(839,170)	29,503
Total	(5,103,916)	-	(10,625,444)	119,850	(1,295,593)	(11,801,187)

¹ The Utility opening balance includes an increase of \$892 from \$4,909,975 and the Industrial opening balance includes a decrease of \$12,395 from \$3,724,537. The increase in Utility and the decrease in Industrial is the effect on prior years balances of billing adjustments on January's bill relating to Abitibi Grand Falls and Stephenville for the period July to December 2004.

Newfoundland and Labrador Hydro Assessable Revenue (\$ 000s)		
Year Ended December 31		
	2005	2004
Electricity Sales	404,212	390,758
Rate Stabilization	56,494	34,187
Other Revenue	2,253	2,240
	462,959	427,185
Deduct:		
Hydro Quebec Sales	49,337	44,142
Iron Ore Company of Canada	4,980	3,993
Wabush Mines	6	-
Interest on Short Term Investment	1	-
Input Tax Credits	145	-
Insurance Refund of Loss on Rencontre East Fire	-	380
Error in Accrual of Rental Revenue From Aliant	-	(148)
Assessable Revenue	408,490	378,818

NEWFOUNDLAND & LABRADOR HYDRO
2005 Annual Report on the Rural Deficit

	2005 Actual			
	Revenues	Cost of Service Before Deficit and Revenue Allocation	Revenue Credits	Deficit
	(\$)	(\$)	(\$)	(\$)
Rural Deficit Areas				
Island Interconnected	34,671,515	49,108,973	(99,629)	(14,337,829)
Island Isolated	1,364,969	8,505,224		(7,140,254)
Labrador Isolated	4,949,452	21,623,155		(16,673,703)
L'Anse au Loup	1,539,865	3,072,856		(1,532,991)
DND Revenue Credit			(2,540,916)	2,540,916
Total	42,525,802	82,310,207	(2,640,546)	(37,143,860)

	2005 Actual ⁽¹⁾				
	Number of Communities ⁽²⁾	Number of Customers	Cost per kWh ⁽³⁾	Deficit per Customer ⁽³⁾	Cost Recovery Ratio ⁽³⁾
			(\$)	(\$)	
Rural Deficit Areas					
Island Interconnected	144	22,002	0.14	(652)	0.71
Island Isolated	8	937	0.95	(7,620)	0.16
Labrador Isolated	17	2,376	0.66	(7,018)	0.23
L'Anse au Loup	8	956	0.21	(1,604)	0.50
Total	177	26,271	0.20	(1,414)	0.52

	Forecast Deficit (\$)				
	2006	2007	2008	2009	2010 ⁽⁴⁾
Rural Deficit Areas					
Island Interconnected	16,095,000	15,371,000	18,299,000	20,143,000	20,847,000
Isolated Systems	24,456,000	24,426,000	25,130,000	25,664,000	25,924,000
DND Revenue Credit	(2,401,000)	(3,041,000)	(3,647,000)	(3,557,000)	(3,480,000)
Total	38,150,000	36,756,000	39,782,000	42,250,000	43,291,000

⁽¹⁾ Average cost for Island Interconnected customers less Rural Interconnected is \$0.044 per kilowatthour and cost for Labrador Interconnected customers is \$0.018 per kilowatthour. Both calculations are based on kW.h sales.

⁽²⁾ Hydro's definition of Community corresponds to the "Town Code" in its customer information system. Some smaller communities may be combined if they share a single postal code.

⁽³⁾ Excludes DND Revenue Credit.

⁽⁴⁾ Operating and maintenance costs are projected to increase by inflation and no base rate increases have been assumed.

Specific initiatives undertaken in 2005

Specific initiatives undertaken in 2005 to reduce the capital and operating costs for the rural systems include:

Centralized Planning

Centralized planning departments with dedicated maintenance planners have been established in Bishop's Falls, Port Saunders, Happy Valley / Goose Bay, Holyrood, and Bay d'Espoir. The overall benefit is that front line personnel can now spend more time in the field or at the work location, allowing better utilization of the workforce, and tighter control of the work activities. As well a review of prioritization practices was undertaken in an effort to ensuring consistency across the organization. As well, efforts were made to ensure that some number of lower priority items were also completed and not left in backlog indefinitely.

Asset Optimization

In our terminal stations Hydro has instituted a program for reclaiming transformer oil with the goal of obtaining increased service life. From 2002 to 2004 Hydro had reclaimed 5 power transformers utilizing contractors, at a cost of approximately \$55,000 per unit. As a result of this significant cost, Hydro purchased an oil reclamation unit in 2005. Even with the initial up front capital cost of approximately \$500,000, the purchase of this unit will save Hydro an estimated \$1,150,000 over a ten-year period, assuming 3 power transformers are reclaimed each year.

In 2004 and 2005 the air blast breaker overhaul program to extend the life of aging 230 kV Air Blast Circuit Breakers was continued. Five breaker overhauls were completed in the past two years.

The frequency for scheduled overhauls on diesel engines has been extended from every 15,000 to every 20,000 hours. This is intended to mitigate operating and maintenance cost pressure without compromising reliability.

Helicopter Usage

In 2005, Hydro was able to reduce hours flown from the previous 3-year average of 1560 hours to 1140 hours. These reductions are attributable primarily to reduced line patrols consistent with Reliability Centered Maintenance (RCM). In addition, a marked decrease in helicopter use by TRO Labrador was accomplished through a greater reliance on regularly scheduled flights where viable. With better planning particularly with respect to Outage Management, better integration of remote site visits will aid in containing helicopter cost.

Automatic Meter Reading

In 2004 and 2005 Hydro conducted a pilot project for Automatic Meter Reading (AMR), which can be a very cost effective and efficient means of reading customer meters. The project proved to be successful and demonstrated that the technology was workable in Hydro's rural service areas. A Business Case was drafted in 2005 to examine the feasibility of expanding AMR. The Business Case will include a plan for implementation in some service areas beginning in 2007, subject to the Board's approval of a pending capital budget proposal.