Financial Statements of

NIAGARA-ON-THE-LAKE HYDRO INC.

December 31, 2011

KPMG LLP
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INDEPENDENT AUDITORS' REPORT

To the Shareholder:

We have audited the accompanying financial statements of Niagara-on-the-Lake Hydro Inc. (the “Entity”), which comprise the balance sheet as at December 31, 2011, and the statements of operations and retained earnings and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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 comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

KPMG

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Niagara-on-the-Lake Hydro Inc. as at December 31, 2011, and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Other Matters

The financial statements of Niagara-on-the-Lake Hydro Inc. for the year ended December 31, 2010, were audited by another auditor who expressed an unmodified audit opinion on those statements on April 26, 2011. We draw attention to Note 2 to the financial statements as at and for the year ended December 31, 2010 which indicates that these financial statements have been restated from those on which they originally reported on April 26, 2011 and more extensively discusses the reason for the restatement.

As part of our audit of the financial statements as at and for the year ended December 31, 2011, we audited the adjustments described in note 2 that were applied to restate the financial statements as at and for the year ended December 31, 2010. In our opinion, such adjustments are appropriate and have been properly applied. We were not engaged to audit, review or apply any procedures to the financial statements of the Entity as at and for the year ended December 31, 2010, other than with respect to the adjustments and, accordingly, we do not express an opinion or any other form of assurance on the financial statements as at and for the year ended December 31, 2010 taken as a whole.

KPMG LLP

Chartered Accountants, Licensed Public Accountants

April 26, 2012
Hamilton, Canada

NIAGARA-ON-THE-LAKE HYDRO INC.

Balance Sheet

December 31, 2011, with comparative figures for 2010

	2011	2010 (Restated note 2)
Assets		
Current assets:		
Cash	$ 567,832	$ 239,382
Accounts receivable	1,638,513	2,236,763
Unbilled revenue	1,196,019	1,666,089
PILs receivable	504,781	309,480
Due from affiliated companies (note 3)	591,079	568,813
Inventories	403,257	218,510
Prepaid expenses	83,202	92,379
	4,984,683	5,331,416
Property, plant and equipment (note 4)	19,940,827	19,822,096
Future PILs	776,084	1,128,644
Regulatory assets (note 10)	2,005,738	179,381
Special deposits	349,467	347,483
Investment (note 5)	10,194	12,395
	$ 28,066,993	$ 26,821,415
Liabilities and Shareholder's Equity		
Current liabilities:		
Demand instalment loans (note 7)	$ 3,601,885	$ 3,838,687
Ontario Infrastructure Projects Corporation loan (note 8)	100,000	1,350,462
Accounts payable and accrued liabilities (note 9)	4,481,077	3,508,090
	8,182,962	8,697,239
Ontario Infrastructure Projects Corporation loan (note 8)	1,316,667	-
Employee future benefits (note 11)	454,343	454,554
Customer deposits	349,467	347,483
Accumulated vested sick leave credits	-	24,509
Note payable (note 12)	5,146,521	5,746,838
Shareholder's equity:		
Share capital (note 13)	2,632,307	2,632,307
Paid-up capital	4,269,026	4,269,026
Retained earnings	5,715,700	4,649,459
	12,617,033	11,550,792
	$ 28,066,993	$ 26,821,415

See accompanying notes to the financial statements.

Signed on behalf of the Board:

________________ Director ________________ Director

NIAGARA-ON-THE-LAKE HYDRO INC.

Statement of Operations and Retained Earnings

December 31, 2011 with comparative figures for 2010

	2011	2010 (Restated note 2)
Service Revenue (note 14)	$ 20,460,616	$ 19,026,653
Cost of power purchased	15,545,062	14,509,994
Gross Margin	4,915,554	4,516,659
Other Income	477,143	403,619
	5,392,697	4,920,278
Other Expenditure:		
Distribution operations	819,343	749,248
Billing and collection	402,377	333,308
General administration	735,752	718,665
Financial expense	760,671	677,459
Amortization (note 18)	1,428,183	1,386,007
	4,146,326	3,864,687
Net income before income taxes	1,246,371	1,055,591
Income Taxes		
Current	(88,838)	99,209
Future	268,968	148,138
	180,130	247,347
Net income for the year	1,066,241	808,244
Retained earnings, beginning of year, as previously reported	5,429,680	4,694,552
Correction of an error (note 2)	(780,221)	(853,337)
Retained earnings, beginning of year, as restated	4,649,459	3,841,215
Retained earnings, end of year	$ 5,715,700	$ 4,649,459

See accompanying notes to the financial statements.

NIAGARA-ON-THE-LAKE HYDRO INC.

Statement of Cash Flows

December 31, 2011 with comparative figures for 2010

	2011	2010 (Restated note 2)
Cash provided by (used in):		
Operating activities:		
Net income for the year	$ 1,066,241	$ 808,244
Amortization (note 18)	1,508,884	1,450,087
Gain on disposal of assets	(53,986)	-
Employee future benefits	(211)	(211)
Accumulated vested sick leave credits	(24,509)	840
Future income taxes	268,968	148,138
Changes in non-cash working capital components (note 15a)	1,648,170	(351,686)
Change in regulatory assets	(1,609,600)	(1,588,851)
Funds provided by operating activities	2,803,957	466,561
Investing activities		
Additions to property, plant and equipment (note 15b)	(1,760,780)	(1,227,078)
Proceeds on disposal of assets	53,986	-
Special deposits, net	(1,984)	11,660
Customer deposits, net	1,984	(11,660)
Other deposits, net	-	(24,180)
Change in other assets	-	1,210
Change in investment	2,201	(3,037)
Funds used in investing activities	(1,704,593)	(1,253,085)
Financing activities		
Demand instalment loans	(236,802)	(111,272)
Repayment of OIPC construction loan	(1,350,462)	1,350,462
Issuance of new debt OIPC loan	1,416,667	-
Repayment of long-term note payable	(600,317)	(549,876)
Funds provided by (used in) financing activities	(770,914)	689,314
Increase (decrease) in cash	328,450	(97,210)
Cash, beginning of year	239,382	336,592
Cash, end of year	$ 567,832	$ 239,382

On July 1, 2000, Niagara-on-the-Lake Hydro Inc. (the "Company") was incorporated under the Business Corporations Act (Ontario) along with its affiliated companies, Niagara-on-the-Lake Energy Inc. and Energy Services Niagara Inc. The incorporation was pursuant to the provisions of the Energy Competition Act, 1998.

1. Significant accounting policies:

These financial statements of Niagara-on-the-Lake Hydro Inc. have been prepared in accordance with Canadian generally accepted accounting principles. The Company is a wholly-owned subsidiary of Niagara-on-the-Lake Energy Inc. The Company has adopted accounting policies prescribed by the Canadian Institute of Chartered Accountants and therefore the financial statements are prepared in accordance with Part V of the CICA Handbook.

(a) Regulation

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

(b) Rate setting

The distribution rates of the Company are based on a revenue requirement that provides a regulated maximum allowable return on equity ("MARE") on the amount of shareholder's equity supporting the business of electricity distribution.

The OEB regulates the electricity distribution rates charged by an Ontario municipal electric utility ("LDC") using a combination of annual incentive rate mechanism ("IRM") adjustments and periodic cost of service reviews. Both such adjustments and reviews are based on applications made by LDC's to the OEB. The current ratemaking policy of the OEB requires a cost of service review every four years, followed by three successive years of IRM adjustments. The Company was approved for a one year extension on their next cost of service review and will file their application in 2014.

1. Significant accounting policies (continued):

(c) Regulatory accounting

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

(d) Inventories

Inventories are measured at the lower of cost, (first in, first out) and net realizable value. Major spare parts and standby equipment are presented as property, plant and equipment as they are used during more than one period.

(e) Property, plant and equipment

Property, plant and equipment are stated at cost and removed from the accounts when disposed or retired. Costs of assets which are pooled are removed from the accounts at the end of their estimated average service lives. Gains or losses at retirement or disposition of such assets are credited or charged to other income.

Amortization is provided for property, plant and equipment using the straight-line method based on the following estimated service lives:

Buildings	25 to 50 years
Transformer stations	40 years
Distribution stations	30 years
Distribution lines	25 years
Distribution transformers and meters	25 years
Other capital assets	3 to 15 years
Intangible assets	20 years

Work in progress assets are not amortized until the project is complete and in service. The Company has not capitalized interest to the cost of assets constructed.

Capital contributions are netted against property, plant and equipment and amortized to income on the same basis as the related asset.

1. **Significant accounting policies (continued):**

(f) Investment

The Company's investment is accounted for using the cost method.

(g) Customer deposits and special deposits

Special deposits are cash collections from customers to guarantee the payment of electricity bills and are classified as a non-current asset. Customer deposits expected to be refunded to customers within the next fiscal period are classified as a current liability.

(h) Employee future benefits

The Company pays certain medical, dental and life insurance benefits on behalf of its retired employees. The Company recognizes these post-retirement costs in the period in which the employees render the services. The excess of net actuarial gains (losses) over 10% of the actual benefit obligation are amortized over the expected average remaining service life of the active employees.

(i) Paid-up capital

Paid-up capital reflects the balance of capital contributions received by the former Niagara-on-the-Lake Hydro-Electric Commission prior to January 1, 2000.

(j) Revenue recognition

Service revenue is recorded as revenue in the period to which it relates. Service revenue from the sale of electrical energy includes an estimated accrual for power supplied but not billed to customers from the last meter reading date to the year end.

(k) Payments in lieu of taxes (“PILs”)

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

Pursuant to the EA, the Company is required to compute taxes under the ITA and OCTA and remit such amounts there under computed to the Ministry of Finance (Ontario).

The Company provides for PILs using the asset and liability method. Under this method, future tax assets and liabilities are recognized, to the extent such are determined likely to be realized, for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases.

Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is

1. **Significant accounting policies (continued):**

(k) Payments in lieu of taxes ("PILs") (continued)

recognized in income in the period that includes the date of enactment or substantive enactment. When unrecorded future income taxes become payable, it is expected that they will be included in the rates approved by the OEB and recovered from the customers of the Company at that time.

PILs recoverable from loss carryforwards are recorded in future PILs on the balance sheet at the current enacted statutory tax rates expected to apply when recovery of the loss carryforwards are expected to be recovered.

(l) Financial instruments

The Company has classified its financial instruments as follows:

Cash is classified as "assets held for trading".

Accounts and other receivables are classified as "loans and receivables".

Demand instalment loans, Ontario Infrastructure Projects Corporation loan, accounts payable and accrued liabilities, customer deposits and note payable are classified as "other financial liabilities".

The Company is required to classify fair value measurements using a fair value hierarchy, which includes three levels of inputs that may be used to measure fair value:

Level I - Quoted prices in active markets for identical assets or liabilities;

Level 2 - Quoted prices in markets that are not active, quoted prices for similar assets or liabilities in active markets or quoted prices that are derived principally from or corroborated by observable market data or other means;

Level 3 - Unobservable inputs that are supported by little or no market activity.

The Company's financial instruments measured at fair value consist of cash which is classified within Level 1 of the fair value hierarchy.

1. Significant accounting policies (continued):

(m) Measurement uncertainty

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

Accounts receivable, unbilled revenue and regulatory assets/liabilities are stated after evaluation of amounts expected to he collected and an appropriate allowance for doubtful accounts. Inventories are recorded net of provisions for obsolescence. Amounts recorded for depreciation and amortization of equipment are based on estimates of useful service life. Employee future benefits are based on certain assumptions, including interest (discount) rate, salary escalation, the average retirement age of employees, employee turnover and expected health and dental care costs.

2. Correction of an error:

Effective January 1, 2009, the Company was required to have adopted the amended sections of Handbook Section 3465 *Income Taxes*.

The amendment to Handbook Section 3465 states that where future income taxes may be expected to be included in approved rates charged to customers in the future and to be recovered or returned to future customers, the recognition of an other asset or other liability for the increase or reduction in future revenue is required. Furthermore, the other asset or other liability established by this requirement is a temporary difference for which an additional future income tax asset or liability is recognized. This change has been applied on a retroactive basis with restatement. As a result of this change, opening retained earnings for 2010 decreased by $853,337, regulatory assets decreased by $1,040,295 and future PILs increased by $260,074. The impact on the Company’s results from operations for the year ended December 31, 2010 was a reduction of future income taxes of $73,116.

3. Due From Affiliated Companies:

	2011	2010
Niagara-on-the-Lake Energy Inc.	$ 5,016	$ 4,655
Energy Services Niagara Inc.	586,063	564,158
	$ 591,079	$ 568,813

The balance due from Niagara-on-the-Lake Energy Inc. is non-interest bearing with no fixed terms of repayment. The balance due from Energy Services Niagara Inc. bears interest at a variable rate and at year end was prime plus 0.15%. Interest charged for the year amounted to $17,961 (2010 - $22,641).

4. Property, Plant and Equipment:

			2011	2010
	Cost	Accumulated amortization	Net book value	Net book value
Land	$ 307,134	$ -	$ 307,134	$ 307,134
Buildings	1,013,925	352,085	661,840	660,593
Transformer stations	5,411,028	981,570	4,429,458	4,553,183
Distribution stations	160,630	109,630	51,000	54,064
Distribution overhead lines	11,153,804	6,772,155	4,381,649	4,538,386
Distribution underground lines	11,624,521	5,944,951	5,679,570	5,773,796
Distribution transformers	5,609,426	3,189,633	2,419,793	2,488,060
Distribution meters	713,118	472,499	240,619	396,222
Equipment and trucks	4,165,742	3,118,741	1,047,001	1,028,532
Other	25,038	13,979	11,059	12,311
Work in progress	711,704	-	711,704	9,815
	$ 40,896,070	$ 20,955,243	$ 19,940,827	$ 19,822,096

Included in property, plant and equipment are intangible assets totaling $25,038 (2010 - $25,038) with a net book value of $11,059 (2010 - $12,311).

5. Investment:

	2011	2010
100 common shares of Utility Collaborative Services Inc. ("UCS") - at cost	$ 100	$ 100
Payments and costs incurred on behalf of UCS	10,094	12,295
	$ 10,194	$ 12,395

In 2009, the Company acquired a 12.5% interest in UCS. The purpose of this company is to provide billing system support services for the Company.

6. Related Party Transactions:

During the period, Niagara-on-the-Lake Hydro Inc. provided operation and administration services to its affiliates in the normal course of business in the following amounts:

	2011	2010
Energy Services Niagara Inc.	$ 223,613	$ 233,692

In the ordinary course of business, the Company enters into transactions with the Town of Niagara-on-the-Lake (the "Town") including its boards and agencies. The Company derives revenues from the sale of electricity and recovers costs of supplying electrical equipment and distribution system from these related parties. Purchases from related parties are measured at the exchange amount of consideration established and agreed to by the related parties. Account balances resulting from these transactions which are included in the balance sheet are settled in accordance with normal trade terms.

Interest paid on the long-term note payable is disclosed in note 12.

7. Demand Instalment Loans:

	2011	2010
Demand instalment loan, bearing interest at prime plus 0.75 %, repayable in monthly instalments of $15,556, due August 2013	$ 1,728,146	$ 1,890,776
Demand instalment loan, bearing interest at prime plus 0.75 %, repayable in monthly instalments of $13,333, due August 2015	1,873,739	1,947,911
	$ 3,601,885	$ 3,838,687

The security for the demand instalment loans, operating line, and letters of credit is a general security agreement in the first position, including an assignment of accounts receivable and inventories and a floating charge over all tangible properties subject to a third party agreement with Ontario Infrastructure Projects Corporation limiting this interest to $7,500,000 in specific borrowings. There are unlimited guarantees provided by Niagara-on-the-Lake Energy Inc. and Energy Services Niagara Inc. Finally, an assignment and postponement of claim provided by the Corporation of the Town of Niagara-on-the-Lake in an amount that is unlimited.

Repayment terms for the demand instalment loans have been negotiated for an amortization period of fifteen years. The principal payments due over the next five years are as follows:

2012	$ 344,118
2013	362,890
2014	382,686
2015	403,562
2016	425,577

8. Ontario Infrastructure Projects Corporation ("OIPC") Loan:

This is a construction loan bearing interest between 0.95% and 1.75% for the period, interest only repayable monthly and due December, 2014 or until such time as it is converted into a debenture loan. The security for the loan is a general security agreement in the second position, including an assignment of accounts receivable, inventories, equipment, chattel paper, instruments and securities, intangibles, books and accounts, real property and proceeds. In addition, guarantees have been provided by Niagara-on-the-Lake Energy Inc. and Energy Services Niagara Inc.

In 2011, the Company completed the drawings on this construction loan of $1,500,000. The Board of Directors then approved the conversion to a debenture loan which is to bear interest at 4.27%, repayable in monthly principle instalments of $8,333 plus interest and due February 16, 2026. At December 31, 2011 the outstanding balance of this loan is $1,416,667.

Repayment terms for the OIPC Loan have been negotiated for an amortization period of fifteen years. The principal payments due over the next five years are as follows:

2012	$ 100,000
2013	100,000
2014	100,000
2015	100,000
2016	100,000

9. Accounts payable and accrued liabilities:

Accounts payable and accrued liabilities also includes $1,386,572 (2010 - $594,145) due to the Town of Niagara-on-the-Lake. These payables arose from water and wastewater billings.

10. Regulatory Assets:

The OEB has established in its Electricity Distribution Rate Handbook and its Accounting Procedures Handbook for Electricity Distribution Utilities provisions for recording deferral and variance account regulatory assets or liabilities on the Company's balance sheet. Deferral and variance account regulatory assets/liabilities primarily represent costs that have been deferred in anticipation of future cost recoveries as determined by the OEB.

Settlement variances represent amounts that have accumulated since January 1, 2007 and are comprised of:

– variances between amounts charged by the Independent Electricity System Operator ("IESO") for the operation of the wholesale electricity market and grid, various wholesale market settlement charges and transmission charges, and the amounts billed to customers by the Company based on OEB approved wholesale market service rates

– variances between the amounts charged by the IESO for energy community costs and the amounts billed to customers by the Company based on OEB approved rates

Smart meter deferral accounts are comprised of the deferral of operating expenditures, capital expenditures and revenues related to Smart meters in accordance with direction set out by the OEB. Smart meters permit consumption to be recorded within specific time intervals and specific tariffs to be levied within such intervals.

10. Regulatory Assets (continued):

As part of the OEB's 2009 rate application process, the recovery through distribution rates of specific amounts of the Company's deferral and variance account regulatory asset balances as at December 31, 2007 was approved and is to be recovered over a four year period commencing May 1, 2009.

As part of the OEB's 2010 rate application process, the recovery through distribution rates of specific amounts of the Company's deferral and variance account regulatory asset balances as at December 31, 2008 was approved and was recovered over a one year period commencing May 1, 2010.

As part of the OEB's 2011 rate application process, the recovery through distribution rates of specific amounts of the Company's deferral and variance account regulatory asset balances as at December 31, 2009 was approved and is to be recovered over a one year period commencing May 1, 2011.

As at December 31, 2011, the Company has accumulated $2,005,738 (2010 - $179,381) in net regulatory assets on the balance sheet. It is management's belief that these assets are consistent with the OEB's deferral criteria.

	2011	2010
Deferred PILS variances	$ 316,682	$ (110,085)
Settlement variances	575,838	(349,980)
Renewable generation connection and Smart grid development deferral accounts	384,290	287,804
Other deferral accounts	(132,009)	(20,537)
Smart meter deferral accounts	1,684,475	1,412,474
Stranded meters	133,165	-
Regulatory liability for future taxes	(956,703)	(1,040,295)
	$ 2,005,738	$ 179,381

11. Employee Future Benefits:

Defined Benefit Plan Information

	2011	2010
Accrued benefit obligation, beginning of year	$ 369,721	$ 366,223
Expense for the year	12,181	12,181
Interest expense	18,247	18,247
Benefits paid during the year	(26,930)	(26,930)
Accrued benefit obligation, end of year	373,219	369,721
Unamortized actuarial gain	81,124	84,833
Employee future benefits liability	$ 454,343	$ 454,554

An actuarial valuation was done for the year ended December 31, 2009.

Amortization of the actuarial gain was $3,709 (2010 - $3,709).

The main actuarial assumptions employed for the valuation are as follows:

General Inflation - Future general inflation levels, as measured by changes in the Consumer Price Index (CPI), were assumed at 2.0% in 2009 and thereafter.

Interest (Discount) Rate - The present value of future liabilities and the expense were determined using discount rates of 5.0%.

Salary Levels - Future general salary and wage levels were assumed to increase at 3.3% per annum.

Medical Costs - Medical costs were assumed to be 9% for 2009, decreasing by approximately 0.65% annually until 2015 where it has been graded down to 5% and 5% thereafter.

Dental Costs - Dental costs were assumed to be 5% in 2009 and thereafter.

12. Long-Term Note Payable:

Long-term note payable to the Town of Niagara-on-the-Lake, bears interest at 7.25%, amounts paid and accrued for the year amounted to $400,031 (2010 – $450,475). During the year, there were repayments of $600,317 (2010 – $549,876) to the Town. The long-term note payable is unsecured and there are no fixed terms of repayment.

13. Share Capital:

Authorized
Unlimited number of common shares

	2011	2010
Issued		
1,001 common shares	$ 2,632,307	$ 2,632,307

14. Service Revenue:

	2011	2010
Residential energy	$ 6,826,336	$ 6,596,290
General <50kW energy	3,579,691	3,377,535
General >50kW energy	6,306,823	5,578,588
Unmetered scattered load energy	17,559	16,149
Street lighting energy	225,124	196,171
Sales for retailers	807,061	993,949
Non-competitive charges	2,698,022	2,267,971
Service revenue	$ 20,460,616	$ 19,026,653

15. Statement of Cash Flows:

(a) Changes in working capital components include:

	2011	2010
Accounts receivable	$ 598,250	$ (495,091)
Unbilled revenue	470,070	67,091
PILs receivable	(195,301)	(372,308)
Due from affiliated companies	(22,266)	241,984
Inventories	(184,747)	(326)
Prepaid expenses	9,177	(13,883)
Accounts payable and accrued liabilities	972,987	220,847
	$ 1,648,170	$ (351,686)

15. Statement of Cash Flows (continued):

(b) Acquisition of capital assets

During the period, capital assets were acquired in the amount of $2,206,446 (2010 - $1,527,248). Capital contributions received from third parties amounted to $445,666 (2010 - $300,170). Cash payments of $1,760,780 (2010 – 1,227,078) were made to purchase capital assets.

Meters that were stranded as a result of Smart meter implementation in the amount of $133,165 (2010 - $nil) have been moved to regulatory assets in accordance with OEB guidelines.

(c) Interest and payments in lieu of taxes

	2011	2010
Interest received	$ 8,029	$ 5,065
Interest paid	648,125	633,066
Payments in lieu of taxes paid	111,463	471,517

16. Pension Agreement:

The Company makes contributions to the Ontario Municipal Employees Retirement Systems ("OMERS"), which is a multi-employer plan, on behalf of approximately 19 members of its staff. The plan is a defined benefit plan which specifies the amount of the retirement benefit to be received by the employees based on the length of service and rates of pay.

The amount contributed to OMERS for 2011 was $105,143 (2010 - $90,135) for current service.

17. General Liability Insurance:

The Company is a member of the Municipal Electric Association Reciprocal Insurance Exchange ("MEARIE") which is a pooling of general liability insurance risks. Members of MEARIE would be assessed, on a pro-rata basis, based on the total of their respective deposit premiums should losses be experienced by MEARIE, in excess of reserves and supplementary insurance, for the years in which the Company or the former Niagara-on-the-Lake Hydro-Electric Commission was a member.

Participation in MEARIE covers a three year underwriting period which expires January 1, 2013. To December 31, 2011, the Company has not been made aware of any additional assessments.

18. Amortization:

	2011	2010
Amortization		
Amortization of capital assets charged to operations	$ 1,428,183	$1,386,007
Amortization of capital assets charged to operating assets	80,701	64,080
	$ 1,508,884	$1,450,087

19. Financial Instruments:

Recognition and Measurement

The fair value of cash, accounts receivable PILs receivable, due from affiliated companies, special deposits, accounts payable and accrued liabilities, demand instalment loans and customer deposits correspond to their carrying values due to their short term maturity.

It is not practicable to determine the fair value of the note payable to the Town of Niagara-on-the-Lake due to the limited amount of comparable market information available.

The OIPC Loan has a carrying value of 1,416,667 and fair value of approximately $1,518,000 for current rates of interest for similar instruments with similar maturity dates.

Credit Risk

The Company in the normal course of business monitors the financial condition of its customers and reviews the credit history of new customers. The Company is currently holding customer deposits on hand in the amount of $349,467 (2010 - $347,483) which are reflected on the balance sheet. Allowances are also maintained for potential credit losses. Management believes that it has adequately provided for any exposure to normal customer credit risk.

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's approach to managing liquidity risk is to ensure that it always has sufficient cash and credit facilities to meet its obligations when due.

The Company manages this risk by developing cash forecasts as well as the annual preparation of a 12 month operating plan and the annual preparation of a 60 month capital plan.

Interest Rate Risk

The Company has entered into two fair value swap transactions, with the intent of fixing the interest rate on the first $1,890,776 demand instalment loan at 6.03% and the second $1,947,911 demand instalment loan at 5.38% to the final maturity dates of August, 2018 and October, 2020 respectively.

The fair value of the interest rate swap agreements are based on amounts quoted by CIBC to realize favourable contracts or settle unfavourable contracts, taking into account interest rates as at December 31, 2011. At December 31, 2011 the interest rate swap was in a net unfavourable position of $445,025 ($355,511 - 2010). This unfavourable amount has been included in the demand instalment loan balance. In 2010, the Company monetized the "optionality" component of the swap and received $200,800 in lieu of giving up the right to paydown the swaps before their maturity date. This amount was charged to the fair value component of the swap in 2010. Therefore, the net current year impact of the change in fair value of the interest rate swap included in the statement of operations is an increase (decrease) in financial expense of $89,514 (2010 - $(2,635)).

The Company is also exposed to fluctuations in interest rates relating to the interest rate swap agreements. An increase or decrease of 1% on the agreements would result in interest expense being higher or lower by $33,000.

19. Financial Instruments (continued):

Operating Line of Credit

As at December 31, 2011, the Company had a line of credit of $2,000,000 of which NIL had been drawn down. The line of credit consists of revolving operating and term facilities that bear interest at prime rate plus 0.15% and are covered under the security issued for the demand instalment loans as described in note 7.

Letters of Credit/Guarantees

The Company had arranged for a total letter of credit or guarantee in the amount of $1,200,000. As at December 31, 2011, $1,181,408 is available to the IESO of which NIL had been drawn upon. This is to provide a prudential letter of credit in support of the purchase of electrical power from the IESO. Any draw under this facility will be converted into a capital loan facility with a monthly repayment program to be negotiated. This facility is covered under the security issued for the demand instalment loans as described in note 7.

20. Capital Management:

The Company's main objectives when managing capital are to:

- ensure ongoing access to funding to maintain and improve the electricity distribution system
- meet any capital needs of its other related companies should the need arise
- ensure compliance with covenants related to its credit facilities, demand loan payable and the Town note payable

The Company's definition of capital includes shareholder's equity and long term debt which includes demand instalment loans, OIPC loan and the long-term note payable. As at December 31, 2011 shareholder's equity amounts to $12,617,033 (2010 - $11,550,792) and long-term debt amounts to $10,165,073 (2010 - $10,935,987). The Company's capital structure as at December 31, 2011 is 45% debt and 55% equity (2010 - 47% debt and 53% equity). There have been no changes in the Company's approach to capital management during the year.

21. Emerging Accounting Changes:

Transition to International Financial Reporting Standards (“IFRS”)

The Canadian Accounting Standards Board (“AcSB”) has adopted a strategic plan that will have Canadian GAAP converge with IFRS, effective January 1, 2011 which will require entities to restate, for comparative purposes, their interim and annual financial statements and their opening financial position.

In October 2010, the AcSB approved the incorporation of a one year deferral of adoption of Part 1 of the CICA Handbook for qualifying entities with activities subject to rate regulation. Part 1 of the CICA Handbook now specifies that first-time adoption, for companies that meet this requirement, is mandatory for interim and annual financial statements relating to annual periods beginning on or after January 1, 2012.

The amendment also requires entities that do not prepare its interim and annual financial statements in accordance with Part 1 of the Handbook during the annual period beginning on or after January 1, 2011 to disclose that fact.

21. Emerging Accounting Changes (continued):

In March 2012, the AcSB extended the deferral of adoption of Part 1 of the CICA Handbook for qualifying entities with activities subject to rate regulation for an additional year, beginning January 1, 2013. The Company had decided to implement IFRS commencing January 1, 2012 and management is now assessing whether the extended deferral option will be taken.

22. Comparative figures:

Certain 2010 comparative figures have been reclassified to conform with the financial statement presentation adopted for the current year.