AT THE HEART OF ONTARIO'S POWER SYSTEM

2003 Annual Report

IMO Independent Electricity Market Operator

The IMO's job is to manage Ontario's power needs

We ensure a reliable supply of electricity and direct its flow to communities and businesses across the province

We are the hub where generators sell electricity and where local utilities and companies buy it

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1 FORECASTING
demand throughout Ontario

2 DETERMINING
how much energy is available from generators and importers and how much can be delivered on the transmission system

IMO

3 BALANCING
supply and demand at the best possible price

4 DISPATCHING
instructions to suppliers to provide power

5 MONITORING
actions in the market, billing utilities and large consumers, and paying suppliers

The Independent Electricity Market Operator runs 24 hours a day, seven days a week, forecasting demand and managing electricity supplies to meet the needs of Ontarians.

SUPPLIERS

Generators/ Importers
send energy into the power grid following IMO instructions

Large Volume Users
cut back on their energy use to lower demand

TRANSMITTERS AND DISTRIBUTORS

Transmitters
deliver energy to local utilities and companies directly connected to the grid

Local Utilities
send electricity from the grid to customers in their distribution area

CONSUMERS

Business Customers
who use more than 250,000 kWh a year pay wholesale prices

Residential Customers
and other organizations pay fixed rates

We are at the heart of Ontario's power system

2003 Highlights

- More than $10 billion worth of electricity moved through the IMO-administered electricity market and the IMO was in full compliance with international reliability rules.
- We played a key role in emergency planning and power system restoration during the August blackout that affected 50 million people in Ontario and the northeastern United States. Our training program is widely viewed as a model for other electricity organizations.
- Our rates to operate the market were unchanged for the third year in a row and we maintained sound financial management over the IMO's activities.
- Many new market initiatives, such as the Hourly Generator Output and Capability Reports, were introduced to improve fairness, efficiency and transparency.
- Our 24-hour-a-day, seven-day-a-week operations ensured Ontario businesses and residences continued to enjoy a reliable supply of electricity.

From the Chairman and the CEO

The IMO is a young organization charged with the responsibility for operating the wholesale electricity market and managing the reliability of Ontario's electricity grid. Since we were established five years ago we have met or exceeded electricity industry reliability standards. Never has the importance of this responsibility been so critical as it was during the August 14, 2003 blackout.

With 50 million people affected, including 10 million Ontario residents, it was by far the largest single electricity outage that North America has ever experienced.

The blackout was caused by incidents that arose outside Ontario but, without warning, quickly spread to our province. The IMO was at the centre of the restoration efforts.

Throughout those trying summer days and nights, IMO employees demonstrated the poise and expertise that have earned them high marks at home and in the international community. Through their actions, our employees have gained the trust of Ontarians and industry participants and observers in both Canada and the United States as this province's Reliability Authority. Our training and emergency planning paid off.

James C. Baillie
Chairman

Working with generators, transmitters and other key industry participants, the IMO directed the restoration of Ontario's power system, with almost every customer having power restored by midnight the next day.

The blackout was a dramatic demonstration of the interconnectedness of the electricity system and the importance of both the IMO's role in dealing with inter-jurisdictional agencies, and of having an independent organization carry out that mission.

Our response to the August 14 blackout was only one of a number of highlights for the IMO in 2003. Many new market initiatives, such as the Hourly Generator Output and Capability Reports, were introduced to improve fairness, efficiency and transparency. More than $10 billion worth of electricity moved and was successfully settled through the IMO-administered electricity market.

Dave Goulding
President and Chief Executive Officer

The market once again delivered a number of benefits to Ontario. While there are challenges ahead, we believe that the competitive marketplace is making a major contribution to the efficiency of Ontario's electricity sector and that it will continue to be a successful part of Ontario's electricity picture for many years to come.

THE 2003 BLACKOUT

Ralph Williams (pictured on cover) didn't have time to appreciate the magnitude of the blackout on August 14, 2003 ... he was too busy dealing with it.

Williams is a Superintendent-Operations in the IMO Control Room, the 'nerve centre' of Ontario's electricity system. It is in this control room that the IMO directs the flow of electricity from the more than 100 generating stations through the high voltage transmission system to millions of Ontarians across the province.

Although the IMO's emergency backup power system kicked in immediately following the blackout allowing the control room operations to continue, it

quickly became apparent that this was a large-scale cascading outage affecting more than Ontario. More than 50 million people in parts of Canada and the U.S. were without electricity as a result of incidents originating in Ohio. It took less than 12 seconds for these series of events to cascade into the largest single electricity outage in North America's history.

Approximately 600 generating stations and hundreds of thousands of kilometres of transmission lines were shut down in mere seconds.

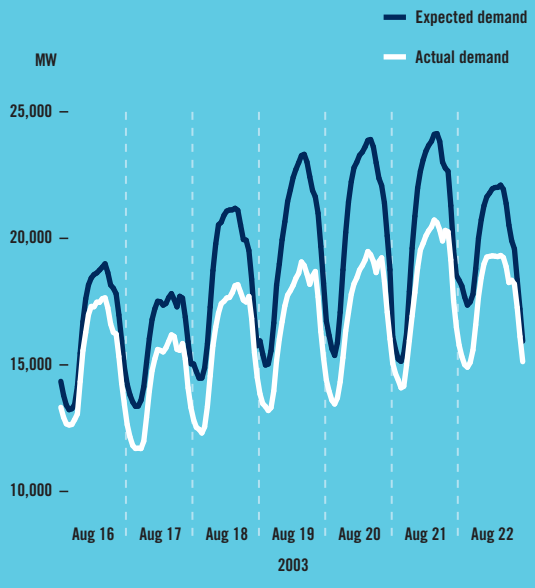
All of this occurred without warning shortly after 4:10 p.m. on that Thursday in August. But Williams and the rest of the control room staff were quick to take action.

"Everyone knew what had to be done and just did it."

Ontarians Heed the Call to Reduce

Within 30 hours from the start of the black-out, power was restored throughout most of the province. For the following seven days, however, the call went out for Ontarians to conserve electricity while generators restarted production. During the peak hours of the day, electricity demand was reduced between 15 to 20 per cent as industry, business and residential users cut back on consumption. This effort was critical in preventing rotating blackouts until all systems returned to normal operation.

ONTARIO DEMAND LOWER DURING EMERGENCY



Continued from page 5

"Within minutes we had quickly changed our thinking from 'Is this really happening?' to 'let's focus on what we have available to start re-energizing the system'," Williams recalls.

The IMO plans for and regularly simulates events such as this one as part of the Ontario Power System Restoration Plan—a plan that was instrumental in restoring electricity service.

Following the blackout, the IMO determined that two hydroelectric generating facilities in Niagara Falls and Cornwall were able to continue operating throughout the event. It was from these two stations that the IMO began the methodical, controlled and orderly process of restoring power in Ontario, continuously maintaining the balance between generation and demand to prevent any further collapse.

Eventually four paths were utilized: from the Niagara Falls and Cornwall area stations as well as from a small generating station in eastern Ontario and several other hydroelectric stations north of Timmins that continued to operate.

As generating stations became operational and transmission lines from those stations were energized, customer load was

Photos, left to right: CP/Peterborough Examiner/Clifford Skarstedt; Toronto Star/Vince Talotta; Reuters/Chris Wattier

restored. This process continued for 30 hours after the blackout, until Ontario's provincial electricity grid was fully functional.

It would take another week before the provincial emergency was lifted and only after tremendous efforts from industry, business and Ontario residents to curtail electricity use by unprecedented amounts. (See page 6.)

But in those anxious minutes following the blackout, the IMO control room employees demonstrated why the IMO is internationally recognized as a leading reliability authority.

Williams said the operators were able to rely on their training and expertise in dealing with the situation at hand. "There was no sense of panic," recalls Williams. "Everyone knew what had to be done and just did it."

Canada-U.S. Task Force Investigation

Ontario could not have prevented the blackout that cascaded into the province. In fact, the high standards and training employed by the IMO will help prevent similar occurrences from originating in Ontario. The Canada-U.S. Power System Outage Task Force that was established to identify the causes of the blackout and to make recommendations to reduce the likelihood of future outages, recommended that other organizations should have quality training programs like those at the IMO.

The task force identified 46 specific recommendations to prevent future blackouts, the most important of which stressed mandatory reliability standards and their enforceability. Through the IMO, Ontario already has mandatory enforceable reliability standards in place, and meets most of the other key recommendations put forward.

The blackout was a result of inadequacies in training, system monitoring tools and tree trimming under transmission lines in Ohio. The blackout should have been prevented at the source and both Canada and the U.S. are taking action to ensure that our electricity system is more reliable. The IMO continues to be a North American leader in electricity system reliability.

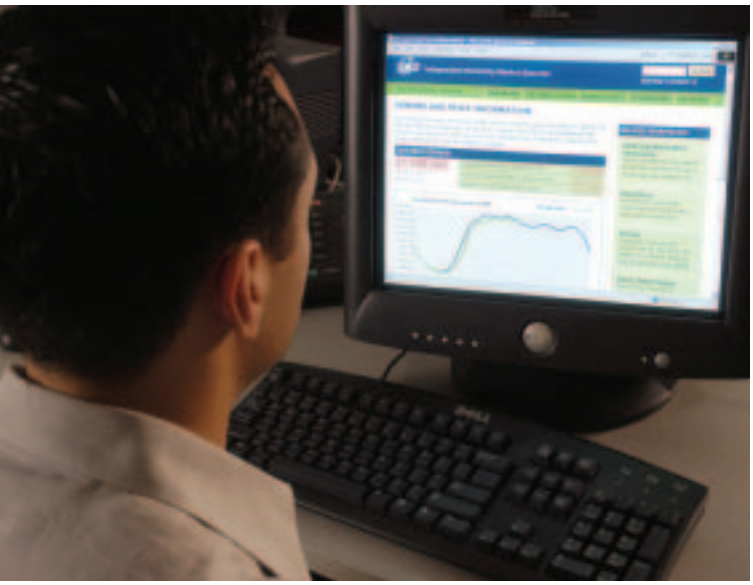
CONSERVING ELECTRICITY
Demand Response

More and more, businesses in Ontario are doing what they can to save money on their energy bills. Many companies closely follow the hourly price of electricity on the IMO website and adjust their consumption when the price gets too high.

Businesses have always kept a close eye on their expenses but the cost of electricity has been less of a concern in the past. However, throughout 2003 most medium and large sized businesses paid the market price for electricity.

The market price for electricity can be more expensive during peak times. Business hours on Monday through Friday and hot and cold days in the summer and winter often see higher prices. Alternatively, electricity prices can be much lower during other periods. Paying the market price for electricity offers businesses the flexibility to manage their electricity costs by reducing their electricity use during the most expensive periods. This type of demand response is new to Ontario, where prior to 2002, electricity prices were flat, regardless of how tight the balance was between supply and demand.

The IMO, through its market relations team, has regular contact with many large users of electricity and they know first hand how companies respond. In fact, organizations can choose to become a dispatchable load in the IMO market. Dispatchable loads provide a bid price to the IMO for a specific amount of their electricity use. If the market clearing price is higher than the bid price the organization is willing to pay then the IMO sends out a dispatch instruction to that organization to stop using electricity in the amount of their bid. Some dispatchable loads accept instructions on a five-minute basis, and some on an hourly basis. There are other benefits to becoming dispatchable such as receiving revenue for providing operating reserve to the market.



Ontario has 465 MW of dispatchable load. That magnitude of demand response enhances system reliability and may give the IMO the flexibility to instruct one less large coal unit to run.

The Ontario government is expanding the role demand response plays in the system by issuing a call for both new generation and demand initiatives to help meet Ontario's long-term electricity needs.

REACHING OUT
Wholesale Customers

Businesses that use more than 250,000 kWh a year pay the wholesale price for electricity, yet not all are aware of how they can use the fluctuating rate to their advantage. The IMO has been working to raise awareness among these consumers about how they can better manage their electricity costs—and to encourage more demand response during peak periods.

Warren Hill, in the IMO's training department has met with businesses that pay the market price for electricity to prompt them to think about how they can lower their electricity bills. At seminars conducted in partnership with local utilities and the Ontario Energy Board, Hill reminds consumers that being price aware and understanding their patterns of electricity use are the starting point for benefiting from the market. Hill asks his audience a number of questions. "Can you shift your load to different times of the day? Can you temporarily reduce load during high-price periods? Can you generate your own electricity? Is your company using electricity as efficiently as possible? Would adding an interval meter be to your advantage?"

These seminars have proven to be extremely helpful to businesses: many have immediately installed interval meters to help control their costs. From the IMO's point of view, this level of awareness will contribute to lower peaks in demand and a more reliable system.

Senior Analyst Cynthia Harrison and Market Development Analyst Paul Berry are developing a transitional program that will increase the level of demand response over the long term.

The Transitional Demand Response Program (TDRP) will be available to large volume customers to help them reduce demand in response to price. The IMO believes such a program is needed to kick-start business efforts to manage electricity use more closely. Customers who sign up for the program will be paid when they reduce demand. These payments are designed to encourage companies to invest in energy management technologies, practices and training. The program, due to be launched in 2004, is another way that the IMO is working to ensure Ontario has an efficient and reliable electricity grid.

STRENGTHENING RELIABILITY
Market Overview

In the year following market opening, the IMO advanced the wholesale electricity market with a number of initiatives that enhanced reliability of the system and improved efficiency and transparency. As we strengthened the foundations of the market, we continued to collaborate with Market Participants to shape its future path.

Spare Generation On-Line

The IMO launched this program to reinforce reliability during periods such as the nighttime and in Spring and Fall when demand is lower. Some fossil-fuel-based generators have long and expensive start-up times and as a result do not make themselves available during these periods, when they are unlikely to be called on to produce electricity. In order to ensure these units are immediately available if there is a sudden increase in demand or decrease in supply, the IMO's Spare Generation On-Line program now offers a guarantee of start-up and minimum costs to eligible generators.

Multi-Interval Optimization (MIO)

The Multi-Interval Optimization program that was approved in 2003 makes the IMO's automated dispatch systems and programs work smarter. Multi-Interval Optimization will better manage the ramping capability (or the ability to increase/decrease output over time) of generators over a longer period of time. This new method of optimizing instructions for generators will be implemented in 2004 and is expected to smooth price, and reduce volatility while managing generation resources more efficiently.

Market Monitoring

The IMO continued its diligent monitoring of the market in 2003 to ensure all Market Participants were complying with the market rules. Ontario's rules already make compliance with reliability standards mandatory and subject to sanction for non-compliance, a key recommendation of the Canada-U.S. Task Force. While not involved in compliance enforcement; the Market Surveillance Panel continued its intensive monitoring of the Ontario market. In its December 2003 assessment of the wholesale electricity market, the Panel reported that "Ontario's electricity market is evolving along the right path to promote the mutually reinforcing goals of market efficiency and system reliability."

IMO Market Participants Atlantic Packaging Products Canada Ltd. (top) and Five Nations Energy Inc. (meeting with IMO's Don Tench)

Generator Output and Capability Reports

Hourly output and capability information from each generator that produces more than 20 MW is now available on the IMO website. Following a request from the Independent Power Producers' Society of Ontario (now Association of Power Producers of Ontario), the IMO Board approved the publishing of this information to promote transparency in the operation of the market.

Hour Ahead Dispatchable Load

In the IMO-administered market, both suppliers and consumers of electricity need to be able to respond to prices for the market to function properly. However there are consumers who can't participate in the market, because they aren't able to change their rate of consumption with only five minutes notice. The Hour Ahead Dispatchable Load program, introduced in 2003, enables more consumers of electricity to respond to price signals by allowing them to act on IMO instructions to reduce consumption on an hourly basis.

REFLECTING TRUE COSTS
Price Highlights

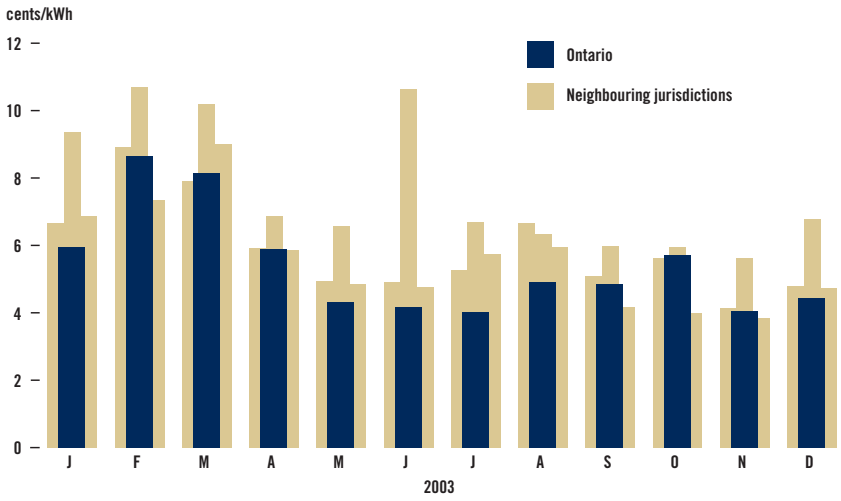
More than $10 billion in electricity flowed through the IMO-administered market in 2003. Roughly half of the electricity was consumed by customers who use a high volume of electricity, while the rest was used by residential and other customers who paid a fixed rate.

High volume users who pay the fluctuating wholesale price for electricity saw lower prices in the latter half of this year due to the more favourable demand/supply scenario in Ontario. The weighted average price of electricity in 2003 was 5.76¢/kWh. Ontario wholesale electricity prices continue to be among the lowest compared to neighbouring jurisdictions of comparable size and fuel mix.

Wholesale electricity prices that typically vary are the most effective way of reflecting the true cost of running a reliable electricity system. Wholesale prices provide a quick means of communicating when it's best to conserve energy and when generators need to produce more.

For 10 months in 2003 the fixed rate of 4.3¢/kWh was less than the fluctuating wholesale rate. The total difference was offset primarily by the Business Protection Plan Rebate funded by Ontario Power Generation. As a result, the net cost of providing a fixed price by the end of 2003 was approximately $850 million, a cost that is borne by the Ontario Electricity Financial Corporation.

WHOLESALE PRICES GENERALLY LOWER IN ONTARIO



Ontario wholesale prices are generally lower than prices in neighbouring jurisdictions that also operate wholesale electricity markets.

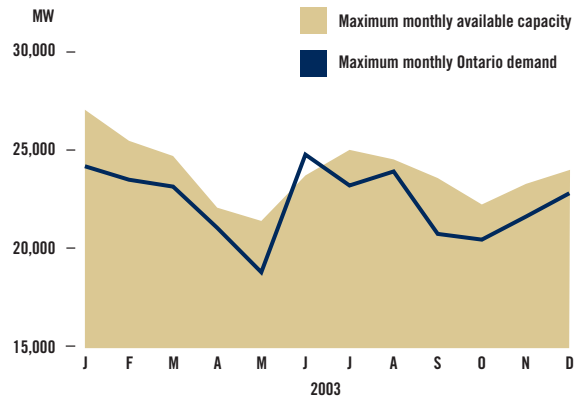
MAINTAINING THE BALANCE
Supply and Demand Highlights

Ontario's electricity supply picture improved significantly in 2003 with the return to service of OPG's Pickering A Unit 4 and Bruce Power's Units 3 and 4, as well as the completion of TransAlta's gas-fired cogeneration facility. These additions, along with increases in capacity at other existing facilities, brought more than 2,500 MW of generating capacity to the system, raising the province's overall installed capacity to 30,500 MW.

At the same time, growth in demand remained relatively flat, even when adjusted for the conservation efforts that took place following the blackout. This was due, in large part, to the mild summer. In July and August 2002, the thermometer rose above 30°C on 20 days. Yet, in 2003, there were only four days that hot. Ontario's peak demand for the entire year was 24,753 MW, 661 MW lower than the all-time record.

Ontario's longer-term demand/supply balance is not as secure. Demand within the province is expected to increase by approximately one per cent each year for the next decade. And by 2014, up to 11,600 MW of Ontario's electricity requirements will need to be met with new supply, refurbished generation or conservation measures. In early 2004, the Ontario Government announced its plans to address this shortfall—including Request for Proposals for new generation capacity and demand-side management initiatives.

MEETING ONTARIO'S ELECTRICITY NEEDS



For system reliability, Ontario requires enough electricity generating capacity to meet the highest peaks in demand. Shortfalls in internal supply are supplemented by imports from neighbouring jurisdictions.

Management's Responsibility for Financial Reporting

The accompanying financial statements of the Independent Electricity Market Operator are the responsibility of management and have been prepared in accordance with accounting principles generally accepted in Canada. The significant accounting policies followed by the Independent Electricity Market Operator are described in the Summary of Significant Accounting Policies contained in Note 2 in the financial statements. The preparation of financial statements necessarily involves the use of estimates based on management's judgement, particularly when transactions affecting the current accounting period cannot be finalized with certainty until future periods. The financial statements have been prepared within reasonable limits of materiality and in light of information available up to February 12, 2004.

Management maintained a system of internal controls designed to provide reasonable assurance that the assets were safeguarded and that reliable information was available on a timely basis. The system included formal policies and procedures and an organizational structure that provided for the appropriate delegation of authority and segregation of responsibilities.

These financial statements have been examined by PricewaterhouseCoopers LLP, a firm of independent external auditors appointed by the Board of Directors. The external auditors' responsibility is to express their opinion on whether the financial statements are fairly presented in accordance with generally accepted accounting principles in Canada. The Auditors' Report, which follows, outlines the scope of their examination and their opinion.

INDEPENDENT ELECTRICITY MARKET OPERATOR

On behalf of management,

Dave Goulding
President and Chief Executive Officer

Gary Sherkey
Vice President – Finance, CFO and Treasurer

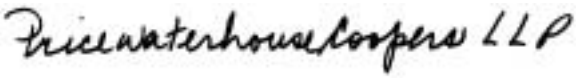
Toronto, Canada
February 12, 2004

To the Board of Directors of the Independent Electricity Market Operator ("IMO")

We have audited the statement of financial position of the IMO as at December 31, 2003 and the statements of operations and accumulated surplus and cash flows for the year then ended. These financial statements are the responsibility of the IMO'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 principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, the financial statements present fairly, in all material respects, the financial position of the IMO as at December 31, 2003, and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.



Chartered Accountants
February 12, 2004

STATEMENT OF OPERATIONS AND ACCUMULATED SURPLUS

(in thousands of Canadian dollars)	FOR THE YEAR ENDED DECEMBER 31, 2003	FOR THE YEAR ENDED DECEMBER 31, 2002
REVENUES		
System fees	$ 148,895	$ 146,650
Other revenue	7,303	2,734
Ancillary services, rural rate assistance and remote subsidies	—	83,436
TOTAL REVENUES	**$ 156,198**	**$ 232,820**
EXPENSES		
Cost of ancillary services, rural rate assistance and remote subsidies	—	83,436
Labour	56,630	52,969
Computer services, support and equipment	10,984	12,548
Consultants, contract and legal services	6,146	4,961
Telecommunications	2,938	7,430
Other costs	5,604	4,661
Amortization	51,160	46,216
TOTAL EXPENSES	**$ 133,462**	**$ 212,221**
Net Income Before Interest and Investment Income	22,736	20,599
Interest and investment income	3,722	2,737
Interest expense and financing charges	(21,535)	(22,225)
NET INCOME FOR THE YEAR	**4,923**	**1,111**
ACCUMULATED SURPLUS — BEGINNING OF YEAR	10,715	9,604
ACCUMULATED SURPLUS — END OF YEAR	**$ 15,638**	**$ 10,715**

See accompanying notes to Financial Statements.

STATEMENT OF FINANCIAL POSITION

(in thousands of Canadian dollars)	FOR THE YEAR ENDED DECEMBER 31, 2003	FOR THE YEAR ENDED DECEMBER 31, 2002
ASSETS		
Current assets		
Cash & cash equivalents	$ 36,939	$ 47,818
Temporary investments	12,442	65,158
Prepaid expenses & receivables	19,344	18,174
	68,725	**131,150**
Property & Equipment (Note 3)		
In service	211,462	237,001
Construction-in-progress	1,664	14,243
	213,126	**251,244**
Other Assets		
Long term investments (Note 4)	6,464	—
Prepaid pension expense (Note 7)	24,566	24,447
	31,030	**24,447**
TOTAL ASSETS	**$ 312,881**	**$ 406,841**
LIABILITIES		
Current Liabilities		
Accounts payable & accrued liabilities (Note 5)	$ 16,431	$ 15,775
Accrued interest	1,952	3,749
Long-term debt payable within one year (Note 6)	—	275,000
	18,383	294,524
Long-term Debt (Note 6)	253,200	78,200
Accrual for Employee Future Benefits Other than Pensions (Note 7)	25,660	23,402
TOTAL LIABILITIES	**297,243**	**396,126**
ACCUMULATED SURPLUS	**15,638**	**10,715**
TOTAL LIABILITIES & ACCUMULATED SURPLUS	**$ 312,881**	**$ 406,841**

See accompanying notes to Financial Statements.

On behalf of the Board:

James C. Baillie

Carol S. Perry

STATEMENT OF CASH FLOWS

(in thousands of Canadian dollars)	FOR THE YEAR ENDED DECEMBER 31, 2003	FOR THE YEAR ENDED DECEMBER 31, 2002
OPERATING ACTIVITIES		
Net income for the year	$ 4,923	$ 1,111
Adjustments for non-cash items:		
Amortization	51,160	46,216
Decrease/(Increase) in prepaid pension expense	4,276	(209)
Increase in accrual for employee future benefits other than pensions	2,258	1,713
	62,617	**48,831**
Changes in non-cash balances related to operations:		
Contribution to pension fund	(4,395)	(135)
Decrease in accounts payable and accrued liabilities	(1,832)	(3,406)
Increase in prepaid expenses and receivables	(1,170)	(11,999)
Decrease in amounts due under Transitional Revenue Allocation Agreement	—	12,626
	(7,397)	**(2,914)**
Cash provided from operating activities	**$ 55,220**	**$ 45,917**
INVESTING ACTIVITIES		
Net sale/(purchase) of temporary investments	52,716	(65,158)
Purchase of long term investments	(6,464)	—
Investment in property & equipment	(12,351)	(49,050)
Cash provided from/(used in) investing activities	**$ 33,901**	**$ (114,208)**
FINANCING ACTIVITIES		
Retirement of long-term debt	(100,000)	—
Cash used in financing activities	**$ (100,000)**	—
NET CHANGE IN CASH & CASH EQUIVALENTS	(10,879)	(68,291)
CASH & CASH EQUIVALENTS — BEGINNING OF YEAR	47,818	116,109
CASH & CASH EQUIVALENTS — END OF YEAR	**$ 36,939**	**$ 47,818**

See accompanying notes to Financial Statements.

Supplementary Information: *(in thousands of Canadian dollars)*

Interest Paid	**$ 23,291**	**$ 23,291**

1. NATURE OF OPERATIONS

Independent Electricity Market Operator (IMO) is a not-for-profit, non-taxable corporation, created by statute effective on April 1, 1999 pursuant to Part II of *The Electricity Act*, 1998. As set out in *The Electricity Act*, the IMO operates pursuant to a license granted by the Ontario Energy Board. The objects of the IMO as contained in *The Electricity Act*, are as follows:

- to exercise and perform the powers and duties assigned to the IMO under *The Electricity Act*, 1998, the market rules and license;
- to enter into agreements with transmitters giving the IMO the authority to direct the operations of their transmission systems;
- to direct the operations and maintain the reliability of the IMO-controlled grid to promote the purposes of *The Electricity Act*, 1998;
- to establish and operate the IMO-administered markets to promote the purposes of *The Electricity Act*, 1998;
- to collect and provide to the public information relating to the current and future electricity needs of Ontario and the capacity of the integrated power system to meet those needs;
- to participate in the development by any standards authority of standards and criteria relating to the reliability of the transmission systems;
- to work with the responsible authorities outside Ontario to co-ordinate the IMO's activities with their activities.

The North American electrical utility industry has undertaken initiatives to move away from traditional monopolies toward introducing competition into power generation. On October 30, 1998 the Government of Ontario enacted the Energy Competition Act, 1998 to restructure the business carried on by Ontario Hydro and introduce competition. On May 1, 2002 the Government of Ontario opened the competitive electricity market.

On December 9, 2002 the Government passed Bill 210, *Electricity Pricing, Conservation and Supply Act, 2002*. Bill 210, among other things, froze the commodity cost of electricity for a portion of the competitive market, specifically low-volume and designated customers, until May 1, 2006 at 4.3 cents per kilowatt hour. On December 15, 2003, the newly elected Government of Ontario passed Bill 4, Ontario Energy Board and Amendment Act, 2003. Under Bill 4, beginning April 1, 2004 low-volume and designated consumers will pay 4.7 cents per kilowatt hour for their first 750 kilowatt hours of consumption and 5.5 cents per kilowatt hour for their remaining monthly consumption. This interim pricing scheme will remain in place until the Ontario Energy Board (OEB) develops an alternative mechanism for setting prices in the future, and no later than May 1, 2005.

The price signals for the wholesale price of energy continue to be set in the market, utilizing methodologies and systems unchanged from those utilized prior to either Bill 210 or Bill 4. In addition, customers that are neither low-volume or designated customers continue to pay market prices, unchanged from prior to the passage of either Bill 210 or Bill 4.

The Electricity Act, specifically Section 19, requires on an annual basis, that the IMO submit its proposed expenditures, revenue requirements, and fees it proposes to charge during the coming year to the OEB for review. Bill 210 amended Section 19 to provide that the submission may be made only with the approval of the Minister of Energy, a requirement that remains unchanged under Bill 4. The IMO obtained permission of the Minister of Energy to submit its proposed expenditures, revenue requirements, and fees to the OEB in October 2003. In December 2003, the OEB approved the IMO's requested 2004 expenditures, revenue requirements, and fees. As specified in *The Electricity Act*, any surplus generated shall be used by the IMO for the purposes of carrying out its objects under *The Electricity Act*. The IMO expects to recover any deficit in future system fees, subject to approval by the Ontario Energy Board.

On January 14, 2004, the Energy Conservation and Supply Task Force released its report to the Minister of Energy entitled "Tough Choices: Addressing Ontario's Power Needs". The task force was established in June 2003 to develop an action plan for attracting new generation, promoting conservation, and enhancing the reliability of the transmission grid. Should the Government of Ontario implement the recommendations of the Energy Conservation and Supply Task Force, there will be significant changes to many aspects of Ontario's electricity industry, including the IMO's roles and responsibilities.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a) Basis of financial statement preparation

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in Canada.

b) Revenue recognition

In accordance with an agreement between the IMO and the other successor entities of Ontario Hydro, the IMO received system fees and ancillary service fees during the period up to market opening on May 1, 2002. Such fees were approved by the Ontario Energy Board (OEB) and were recognized as earned in accordance with the terms of the agreement.

Since the opening of the IMO-administered markets on May 1, 2002, system fees earned by the IMO are based on approved rates for each megawatt of electricity withdrawn from the IMO-controlled grid. System fees are recognized as revenue at the same time as the electricity is withdrawn.

Since market opening, ancillary service transactions became those of the market participants rather than the IMO. These financial statements do not include the financial transactions of market participants within the IMO-administered markets.

Other revenue represents amounts that accrue to the IMO relating to interest on funds passing through market settlement accounts, as well as fines and penalties passing through the market adjustment account. Such revenue is recognized as it accrues.

c) Cash and cash equivalents

Cash and cash equivalents comprise cash, term deposits and other short-term investments with original maturity dates of less than 90 days.

d) Temporary investments

Short-term money market investments with original maturities of 90 days or longer are classified as temporary investments and valued at amortized cost. Premiums and discounts are amortized to income using the constant yield method over the period to maturity.

e) Construction-in-progress

Construction-in-progress generally relates to the costs of physical facilities, hardware and software, and includes costs paid to vendors, internal and external labour, consultants, an applicable share of overhead, and an allocation of interest related to funds borrowed to finance the project. Costs relating to construction-in-progress are transferred to property and equipment in service when the asset under construction is deemed to be ready for use.

f) Property and equipment in service

Property and equipment are capitalized at cost, which comprises materials, labour, external support, overheads, and interest applicable to capital activities.

g) Amortization

The capital cost of property and equipment in service is amortized on a straight line basis over their estimated service lives. The estimated service lives in years, from the date the assets were transferred from Ontario Hydro or subsequently acquired, are:

Class	Estimated Average Service Life
Facilities	41
Market Systems and Applications	4 to 7
Infrastructure and Other Assets	3 to 10

Gains and losses on sales of property and equipment and losses on premature retirements are charged to operations as adjustments to amortization expense. Removal costs are charged to amortization expense as incurred.

The estimated service lives of property and equipment and the significant assumptions underlying the estimates of removal costs are subject to periodic review. The impacts of changes in the estimated lives of property and equipment are amortized on a prospective basis. The most recent review was completed in fiscal 2003.

h) Long term investments

Portfolio investments are carried at cost less any provision for other than temporary losses.

i) Pension and other post-employment benefits

The IMO's post-employment benefit programs include pension, group life insurance, health care, long-term disability and workers compensation benefits.

The IMO accrues obligations under pension and other post-employment benefit ("OPEB") plans and the related costs, net of plan assets. Pension fund assets are valued using market related values for equities, whereby fund assets are calculated using a five-year moving average of year-end market values, and market values for fixed income securities. Pension and OPEB expenses and obligations are determined annually by independent actuaries using the projected benefit method and management's best estimates using a measurement date of September 30.

Pension and OPEB expenses consist of current service costs, interest and adjustments arising from plan amendments, changes in assumptions, and experience gains or losses, which are amortized on a straight line basis over the expected average remaining service life of the employees covered by the plan. Pension and OPEB expenses are recorded during the year in which employees render services.

j) Fair value of financial instruments

The carrying amounts reported in the balance sheet for financial instruments, comprising current assets and current liabilities approximate to their fair values. The fair value of long term investments is disclosed in Note 4. The fair value of the long-term debt is not readily available.

k) Foreign exchange

Transactions denominated in foreign currencies are translated into Canadian dollars at the rate of exchange prevailing on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated in Canadian dollars at the rate prevailing at that date. Exchange gains and losses arising on settlement of foreign exchange transactions are reported in the statement of operations at the date at which the transactions are settled.

l) Use of estimates

The preparation of the financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities and the disclosure of contingent assets and liabilities as at the date of the financial statements. Actual results could differ from those estimates.

3. PROPERTY AND EQUIPMENT

	As at December 31, 2003			As at December 31, 2002
(in thousands of Canadian dollars)	Cost	Accumulated Amortization	Net Book Value	Net Book Value
Property and equipment in service				
Facilities	$ 48,081	$ 5,312	$ 42,769	$ 44,156
Market Systems and Applications	205,070	67,593	137,477	145,423
Infrastructure and Other Assets	66,581	35,365	31,216	47,422
	319,732	108,270	211,462	237,001
Construction-in-progress	1,664	—	1,664	14,243
	$ 321,396	**$ 108,270**	**$ 213,126**	**$ 251,244**

In 2003, adjustments were made to reflect management's estimates of remaining asset service lives. The impact of these changes in estimates was an increase in amortization expense of $7,361,243 in the year.

Removal costs of $1,920,219 related to the Data Acquisition and Computer Systems were incurred in 2003. These costs were charged to amortization in the year.

Interest capitalized to construction-in-progress during 2003 was $356,110 (2002 - $960,331).

4. LONG TERM INVESTMENTS

Long term investments represent an investment in a balanced pooled fund. The market value of these investments was $6,938,338 as at December 31, 2003.

5. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

(in thousands of Canadian dollars)	As at December 31, 2003	As at December 31, 2002
Relating to property and equipment	$ 2,869	$ 2,178
Relating to operations	13,562	13,597
	$ 16,431	**$ 15,775**

6. LONG-TERM DEBT

(in thousands of Canadian dollars)	As at December 31, 2003	As at December 31, 2002
Notes payable	$ 253,200	$ 353,200
Less payable within one year	—	(275,000)
	$ 253,200	**$ 78,200**

(in thousands of Canadian dollars)	As at December 31, 2003	As at December 31, 2002
Notes payable to		
Ontario Electricity Financial Corporation (OEFC)	$ 78,200	$ 78,200
The Province of Ontario	175,000	275,000
	$ 253,200	**$ 353,200**

Note payable to OEFC

The long-term note payable to Ontario Electricity Finance Corporation (OEFC) is unsecured, bears interest at 7.9% per annum and is repayable in full on May 1, 2009. Interest accrues daily and is payable in arrears, in equal semi-annual payments on May 1 and November 1 of each year.

Note payable to Province of Ontario

The long-term note payable to the Province of Ontario is unsecured.

The loan agreement provided for an extension of the original repayment date of November 3, 2003, if on or before October 27, 2003, the IMO was unable to obtain a credit rating, or obtained a credit rating below a specific level, to the earlier of March 31, 2005 or six months after which a credit rating is either received or revised to a specific level.

The IMO exercised the extension option and at the same time entered into a revised loan agreement with the Province of Ontario, repaying $100 million of the outstanding principal on November 3, 2003. Under the revised agreement interest accrues daily at an interest rate equal to the three month floating Bankers' Acceptance rate plus 50 basis points during this period. At December 31, 2003, the interest rate was 3.26%. The revised loan agreement provides the right for the IMO to make prepayments on the outstanding principal at three month intervals, in multiples of $5 million, co-incident with the payment of interest. On February 3, 2004 the IMO repaid a further $25 million.

Credit facility

IMO has an unsecured, committed, and extendible 364-day revolving credit facility agreement with a Canadian chartered bank, under which the bank will make available to the IMO an amount up to $20 million. As at December 31, 2003 and 2002 no balance was drawn on the credit facility. Advances under this facility are available in Canadian dollars by way of prime rate loans or relevant Bankers'

Acceptances rates. Unused portions of this credit facility are subject to a commitment fee of 10 basis points per annum and a Stamping Fee of 30 basis points per annum upon acceptance of each Bankers' Acceptance.

The IMO also has an unsecured, committed, and extendible 364-day revolving credit facility agreement with a banking syndicate, under which the syndicate will make available to the IMO an amount up to $100 million. As at December 31, 2003 and 2002 no balance was drawn on this credit facility. Advances under this facility are available in Canadian dollars by way of prime rate loans or relevant Bankers' Acceptances rates. Unused portions of this credit facility are subject to a commitment fee of 10 basis points per annum and a Stamping Fee of 30 basis points per annum upon acceptance of each Bankers' Acceptance. This facility will mainly be used to fund shortfalls in amounts owed to the IMO by Market Participants for payment to other Market Participants prior to their recovery under the provisions of the market rules.

7. BENEFIT PLANS

The IMO provides pension and other employee future benefits, comprising group life insurance, long-term disability and group medical and dental plans, for the benefit of current and retired employees.

Pension plans

The Independent Electricity Market Operator Pension Plan is a contributory defined benefit, registered pension plan. In addition to the funded, registered, pension plan, the IMO provides certain non-registered defined benefit pensions through an unfunded, non-registered plan.

Other employee future benefits

The group life insurance, long-term disability and group medical and dental benefits are provided through unfunded, non-registered defined benefit plans.

Summary of accrued benefit obligations and plan assets

(in thousands of Canadian dollars)	2003 Pension benefits	2002 Pension benefits	2003 Other benefits	2002 Other benefits
Accrued benefit obligation	$ 272,317	$ 234,967	$ 34,694	$ 28,876
Fair value of plan assets	215,412	203,693	—	—
Funded status	$ (56,905)	$ (31,274)	$ (34,694)	$ (28,876)
Prepaid (accrued) benefit cost recognized in the statements of financial position	$ 24,566	$ 24,447	$ (25,660)	$ (23,402)

Summary of principal assumptions used to calculate benefit costs and obligations

	2003 Pension benefits	2002 Pension benefits	2003 Other benefits	2002 Other benefits
Discount rate	6.1%	6.6%	6.1%	6.6%
Expected return on plan assets	7.25%	7.25%	—	—
Rate of compensation increase	3.5%	3.5%	3.5%	3.5%
Rate of benefit increases	3.0%	3.0%	—	—
Expected average remaining service life of employees	12 years	12 years	12 years	12 years

Hospital and drug costs are assumed to increase by 9.0% in 2004, 8.0% in 2005, 7.0% in 2006, 6.0% in 2007 and by 5.0% per annum thereafter. Dental costs are assumed to increase by 5.0% per annum.

Summary of benefit costs and plan contributions

(in thousands of Canadian dollars)	2003 Pension benefits	2002 Pension benefits	2003 Other benefits	2002 Other benefits
Benefit cost (income)	$ 4,276	$ (209)	$ 3,298	$ 2,639
Employer contributions	123	39	1,008	890
Plan participant's contributions	1,803	1,654	—	—
Benefits paid	9,228	7,833	1,008	890

An employer contribution in the amount of $4.366 million was made to the registered pension plan in December 2003.

8. SEGMENTED INFORMATION

IMO consists of a single business engaged in the operation of the wholesale electricity system in Ontario.

9. COMMITMENTS

Operating commitments

The obligations of the IMO with respect to non-cancellable operating leases over the next five years is as follows:

(in thousands of Canadian dollars)	
2004	$ 2,123
2005	1,755
2006	1,305
2007	994
2008	994

10. COMPARATIVE FIGURES

Certain of the 2002 comparative figures in the financial statements have been reclassified to conform to the 2003 financial statement presentation.

Board of Directors of the Independent Electricity Market Operator

Front Row (Left to Right)

Glenna Carr
President and CEO,
Carr-Gordon Limited

Robert McGavin
Independent Director

James C. Baillie
Chair,
Independent Electricity Market Operator
Counsel, Torys LLP

Dave Goulding
President and CEO,
Independent Electricity Market Operator

Carol S. Perry
President and CEO,
MaxxCap Corporate Finance Inc.

Back Row

Peter Budd
Chair,
Power Budd/Cameron McKenna

Peter Jones
CEO of Diligent Capital Inc.,
Vice-Chairman, Oxbow Equities Corp.

Paul Ferguson
President,
Newmarket Hydro Ltd.

Dale Struthers
President,
Dalmar Associates

John Grant
Professor,
Macro-economics and
Environmental Economics,
University of Toronto

Tom Parkinson
President and CEO,
Hydro One Inc.

Carl Anderson
Independent Director

Bruce Boland
Senior Vice President,
Customer Solutions,
Ontario Power Generation

John LeMay
Project Manager, Energy Conservation,
Inco Limited

Ed Houghton
President and CEO,
Collingwood Utility Services Corp.

Bill Taylor
Vice-President, Eastern Power,
TransCanada Power Marketing Ltd.

IMO Senior Management Team

Dave Goulding
President and CEO

Bruce Campbell
Vice President,
Corporate and Legal Affairs

Derek Cowbourne
Vice President,
Market Services

Bill Limbrick
Vice President,
Information Technology and Infrastructure

Paul Murphy
Chief Operating Officer,
Market Operations and Forecasts

Gary Sherkey
Vice President – Finance,
CFO and Treasurer

Harry Chandler
Director,
Market Assessment and Compliance

Yvonne Murray
Manager,
Internal Audit

Norm Thomas
Director,
Human Resources

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